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Trade and Development Report

Rethinking development in the age of discontent

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Foreword

Looking only at global averages, the world economy in 2024 performed what experts call a “soft landing”, taming inflation without falling into a recession. That is an important achievement. But the Trade and Development Report 2024: Rethinking Development in the Age of Discontent shows the reality is more nuanced. Although some developing economies show promising growth, the overall picture in the global South is one of weak growth, growing exposure to global shocks and the risk of trade fragmentation.

This report forecasts global growth in gross domestic product of 2.7 per cent for 2024 and 2025, marking three consecutive years below the 3 per cent pre-pandemic growth trend. Regionally, South Asia displays the most dynamic growth. The three major powers of the global economy – China, the United States of America and the European Union – are on decelerating or weakened growth trajectories. Despite the context of a turbocharged technological revolution, the much-needed acceleration in economic activity to achieve the Sustainable Development Goals remains elusive for many countries in the global South trapped by a confluence of high debt burdens, financial and resource outflows, weak investment and enforced austerity. Only 1 of the 46 least developed countries is currently meeting the promise of a 7 per cent annual growth target under the global Goals.

In many ways, the world is seeing a further deterioration of the sluggish “new normal” growth that followed the global financial crisis over 15 years ago. But important shifts in geopolitics and economic thinking – including the return of industrial policy, multipolar trade patterns and new technological innovations – signal that globalization itself is at an inflection point. Whether this will lead to a global paradigm that is more favourable to developing countries and the Sustainable Development Goals remains an open question.

This report seeks to answer it head on. Chapters 1 and 2 present our analysis of major economic trends in the global economy, international trade, financial markets, commodities, and capital flows. Chapters 3 and 4 discuss the current pivot of globalization, marked by the changing structure of global trade, technological innovations and the rise of South–South trade. Chapter 5 advocates concrete ideas for a fairer international tax system and a global financial architecture that gives developing countries the policy space they need to adapt and thrive in this new era.

The Trade and Development Report 2024 is a call to action, showing that despite the many challenges we face, there are clear opportunities for sustained per-capita growth for the developing world, particularly in renewable energies and critical minerals, South–South trade and the strategic use of new generation industrial policies. It is an appeal to policymakers, academics and civil society to engage in critical dialogues that find solutions to reduce the fragility and volatility of our current status quo. Above all, the report is a testament to the fact that the future is not something that happens to us – it is something we create, together. As globalization shifts, we must steer it, carefully and deliberately, towards sustainable development.

Rebeca Grynspan
Secretary-General of UNCTAD

Abbreviations

Ad Hoc Committee	Ad Hoc Committee to Draft Terms of Reference for a United Nations Framework Convention on International Tax Cooperation
ADB	Asian Development Bank
BEPS	base erosion and profit shifting
BIS	Bank for International Settlements
BRICS	Brazil, Russian Federation, India, China and South Africa
ECB	European Central Bank
FAO	Food and Agriculture Organization of the United Nations
FIRE	finance, insurance and real estate
GDP	gross domestic product
ICT	information and communications technology
IEA	International Energy Agency
ILO	International Labour Organization
ITC	International Trade Centre
IMF	International Monetary Fund
ODA	official development assistance
OECD	Organisation for Economic Co-operation and Development
OPEC	Organization of the Petroleum Exporting Countries
OPEC+	Organization of the Petroleum Exporting Countries and its allies
PPP	purchasing power parity
United Nations Tax Committee	Committee of Experts on International Cooperation in Tax Matters
UNWTO	United Nations World Tourism Organization
WHO	World Health Organization
WIPO	World Intellectual Property Organization
WTO	World Trade Organization

Explanatory notes

Classification by country

The classification of countries in this report has been adopted solely for the purposes of statistical or analytical convenience and does not necessarily imply any judgement concerning the stage of development of a particular country or area.

There is no established convention for the designation of "developing" and "developed" countries or areas in the United Nations system. This report follows the classification as defined in the UNCTAD Handbook of Statistics 2023 for these two major country groupings (see https://hbs.unctad.org/classifications/, accessed on 10 October 2024), which is based on the classification applied in the "Standard Country or Area Codes for Statistical Use", known as "M49", maintained by the United Nations Statistics Division (see https://unstats.un.org/unsd/methodology/m49/, accessed on 10 October 2024).

For statistical purposes, regional groupings used in this report follow generally those employed in the UNCTAD Handbook of Statistics 2023 unless otherwise stated. The data for China do not include those for Hong Kong Special Administrative Region (Hong Kong SAR), and Taiwan Province of China.

References to "sub-Saharan Africa" in the text or tables include South Africa unless otherwise indicated.

Other notes

The term "dollar" ($) refers to United States dollars, unless otherwise stated.

The term "billion" signifies 1,000 million.

The term "trillion" signifies 1,000,000 million.

The term "tons" refers to metric tons.

Annual rates of growth and change refer to compound rates.

Use of a dash (–) between dates representing years, e.g. 2019–2021, signifies the full period involved, including the initial and final years.

An oblique stroke (/) between two years, e.g. 2019/20, signifies a fiscal or crop year. A dot (.) in a table indicates that the item is not applicable.

Two dots (..) in a table indicate that the data are not available or are not separately reported.

A dash (–) or a zero (0) in a table indicates that the amount is nil or negligible.

Decimals and percentages do not necessarily add up to totals because of rounding.

2024 Trade and development report

Chapter I

The macroeconomics of discontent

Global output growth shows signs of stabilizing at rates below those registered in the years prior to the pandemic, which itself marked a period of unsatisfactory global growth. Current growth trajectories are insufficient to meet global development and climate challenges and goals.

Prevailing global conditions are particularly worrisome in terms of debt dynamics as the combination of low growth and high interest rates exacerbates debt burdens. High public debt ratios in many economies are equally concerning. A hallmark of the new, post-pandemic norm, they heighten the risk of a return to austerity as a policy guideline.

The post-pandemic inflation spike was largely a supply issue, created by bottlenecks in global value chains and excessive concentration in key sectors. Overreliance on prolonged monetary tightening as the sole policy tool to lower inflation has been only partially effective while inflicting undue hardship domestically and internationally.

The post-COVID-19 recovery has seen widespread discontent as higher consumer prices and credit costs eat into household disposable income. Household consumption spending has been suppressed, remaining below pre-pandemic levels in a number of countries. This fuels feelings of economic insecurity in both advanced and developing countries, a factor driving widespread disaffection with globalization.

United Nations

Key policy takeaways

- **The public debt build-up caused by the pandemic as well as the size of investments needed to address prevailing development and climate challenges have made it clear that rebalancing State budgets requires greater revenues.** The path ahead calls for a coordinated move on global taxation, particularly on high-net-worth individuals and large corporations, and to reverse the trickle-down logic that dominated economic policy during the era of hyperglobalization.

- **Greater access to affordable, reliable and longer-term financing options – particularly for the most vulnerable developing countries – is key to adequate public investment in development goals.** To this end, priority policy actions on the international sphere include increased concessional finance through the capitalization of multilateral and regional banks, the issuance of new and the reallocation of existing special drawing rights and the utilization of innovative financial instruments, among other measures.

- **A more balanced policy mix addressing the different forces driving inflationary pressures** would be more effective and entail less "collateral damage". It would include concerted actions to rein in anti-competitive practices, abuses of dominant market positions and corporate concentration in key markets, as well as revisions to the existing regulatory framework for commodity-trading activities.

- **Monetary authorities should deliberate on the wider impacts of their decisions.** Among the factors to consider are the impacts of monetary decisions on debt trajectories and servicing costs, the financing of critically needed investments and financial sustainability. Changes in the criteria and functioning of policymaking need to be embedded in the mandates of monetary institutions.

A. Introduction

For the global economy, 2024 marks a testing moment. On one hand, all regions are registering positive growth rates, and some developing economies, such as India, Rwanda and Viet Nam, are expanding at an accelerated pace. Inflation rates are coming down in advanced and developing economies, albeit slowly and unevenly. Against initial fears, the turbulence that disrupted international financial markets in August 2024 has not translated into a wider financial contagion, although sources of uncertainty remain.

Yet stabilization brings with it a widening sense of discontent. Nearly four years after the COVID-19 shock and 15 years after the global financial crisis of 2008/09, a new normal has emerged for the world economy, characterized by sluggish growth amid a gradual disinflationary process and positive real interest rates. In a major challenge to development, global growth is stabilizing at rates insufficient for countries of the global South to address the economic, social, development and environmental challenges they face.

Controlling spending to stabilize public debt is insufficient given the investments needed to reduce poverty and income inequality.

Trends in economic policymaking feed concerns. Current international conditions are particularly worrisome for debt dynamics as the combination of low growth and high interest rates exacerbates debt burdens (chapter II, section D). High public debt ratios in many economies are equally worrisome. As a hallmark of the new, post-pandemic norm, they heighten the risk of a return to austerity as a policy guideline.

The path ahead requires a coordinated move to increase global taxation on high-net-worth individuals and large corporations.

Austerity, however, is not a solution to the issues confronting the global economy today. Given the build-up of public debt caused by the pandemic and the size of investments needed to manage prevailing development and climate challenges, rebalancing State budgets requires greater revenues. This, in turn, also depends on more dynamic economic growth.

The mantra of controlling spending to consolidate public debt is simply insufficient, given that the global economy urgently needs more investments in universal public services to reduce poverty and income inequality and address the impending climate crisis. Since these investments are often not current priority areas of government expenditure, they are most vulnerable to political pressures aimed at reducing primary fiscal deficits. The path ahead requires a coordinated move to increase the global taxation of high-net-worth individuals and large corporations, reversing the trickle-down logic that dominated economic policy during the era of hyperglobalization.

On the monetary side, the gradual reduction in inflation rates since mid-2022 has occurred without supposedly required commensurate increases in unemployment. This indicates that the post-pandemic inflation spike was largely a supply issue, created by bottlenecks in global value chains (Weber and Wasner, 2023; Stiglitz, 2023) and excessive oligopolistic power in key sectors, notably agrifood and energy (UNCTAD, 2023b). Overly restrictive monetary policy stances, particularly in major advanced economies, risk inflicting undue hardship both at home and abroad. A more gradualist approach, by contrast, would give more time for demand growth to stimulate investment, thereby raising labour productivity and potential output. The expansion of productive

capacity, in turn, would help to alleviate inflationary pressures in the medium term.

Beyond short-term economic policies, industrial policy has returned explicitly to the agenda of advanced economies, particularly in the United States of America. Yet it is still frowned upon as a policy tool in developing economies, on the assumption that the risks outweigh the benefits when a country does not have an appropriate institutional framework. Successful development cases indicate, however, that the sequencing may be the opposite (chapter IV). While industrial policies inevitably create risks, these induce improvements in governance structures and regulatory frameworks that in turn increase the effectiveness and success of industrial policies.

The explicit return to industrial or development strategies requires coordinated climate policies, with scientific indicators pointing to accelerating climate impacts. In 2023–2024, record-high temperatures have occurred around the world, along with more frequent floods and droughts, a continuous degradation of forest and water resources, and deteriorating biodiversity. The easing of climate risks would, among many positive outcomes, reduce inflationary pressures stemming from extreme weather conditions and cut the costs of mitigating climate change.

Overall, the short-term scenario is not a favourable one. Rising geopolitical tensions have pushed environmental concerns and progressive economic policies from the priority list of many Governments (chapter III). In this context, the role of multilateral institutions, such as UNCTAD, is key in pressing for better policy coordination between advanced and developing economies.

In light of these challenges, this report suggests that:

- Elevated public debt burdens and the magnitude of investments needed to address prevailing development and climate challenges make clear that rebalancing State budgets requires greater revenues. The path ahead requires coordinated actions, including to increase global taxation on high-net-worth individuals and large corporations.
- Improved access to affordable, reliable and long-term financing options – particularly for the most vulnerable developing countries – is key in securing adequate public investment towards development goals. Important policy actions on the international sphere comprise increased concessional finance through the capitalization of multilateral and regional banks, the issuance of new and reallocation of existing special drawing rights, and the utilization of innovative financial instruments, among other measures.
- A balanced policy mix that addresses the different forces driving inflationary pressures would be both more effective and entail less “collateral damage”. Such policies include concerted actions to rein in anti-competitive practices, abuses of dominant market positions and corporate concentration in key markets, as well as revisions to the existing regulatory framework for commodity-trading activities.
- Monetary authorities should deliberate on the wider impacts of their decisions. Among the factors to consider are the impacts of monetary decisions on debt trajectories and servicing costs, the financing of critically needed investments and financial sustainability. Such changes in the criteria and functioning of policymaking need to be embedded in the mandates of monetary institutions.

In this chapter, section B presents the global macroeconomic outlook, focusing on the growth of gross domestic product (GDP) and inflation. Section C discusses the burgeoning discontent triggered by high prices in advanced and developing economies. Section D analyses recent trends in and expectations for interest and exchange rates. Section E moves to fiscal policy and describes the impact of the COVID-19 shock on public debt in the Group of 20 economies. Section F presents simulations of functional income distribution and the most recent data on the impact of the pandemic shock on personal income distribution. Section G details the global economic outlook by region.

Industrial policy has returned explicitly to the policy agenda of advanced economies.

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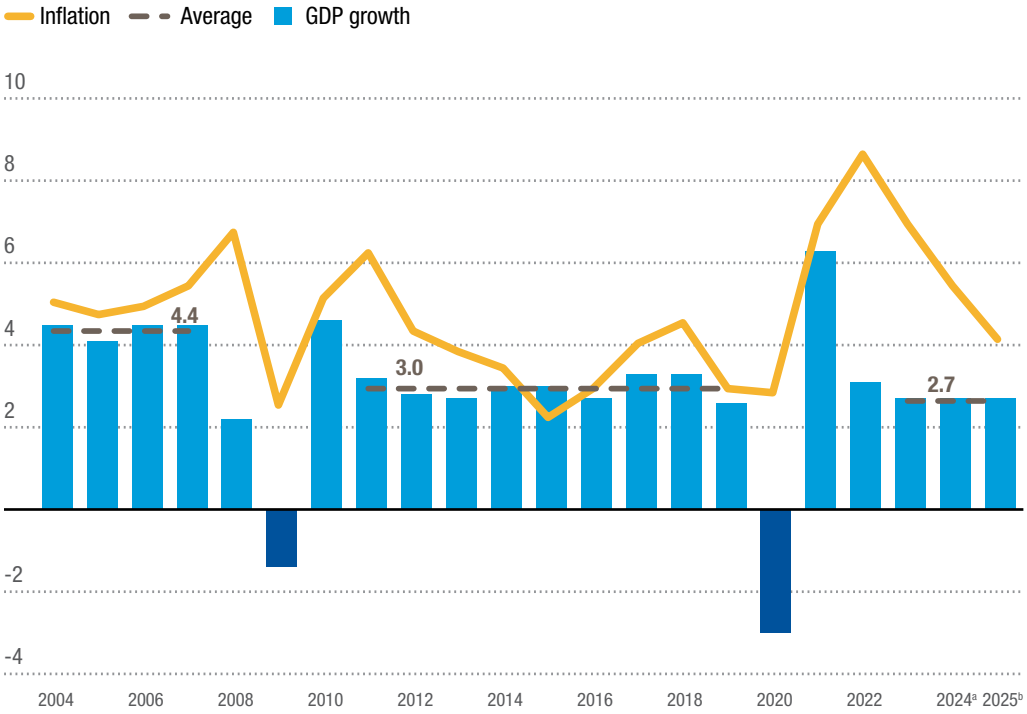
B. Depressed global growth sets in

As stimulus measures to respond to the COVID-19 pandemic were phased out, the primary concern of macroeconomic policy globally became restoring inflation to central bank target ranges. Global output subsequently decelerated from 3.1 per cent in 2022 to 2.7 per cent in 2023. UNCTAD expects the world economy to maintain the same subdued growth rate of 2.7 per cent in 2024 and 2025, marking three years of stable but stagnating growth amid gradual global disinflation (figure I.1 and table I.1).

To put the current situation into historical perspective, the global financial crisis also bore witness to a brief spike in inflation in 2008, albeit of a much smaller magnitude. It led the governments of the largest advanced economies to pursue a "growth-friendly" fiscal consolidation based on the "expansionary fiscal contraction" hypothesis (Alesina and Ardagna, 1998; Jayadev and Konczal, 2010). As a result, fiscal stimulus fell far short of what was necessary to compensate for the shortfall in demand. At the same time, inflation remained below the typical 2 per cent annual target rates in advanced economies.

Figure I.1
Easing inflationary pressures have accompanied lacklustre growth in global output
World output growth and inflation
(Percentage)



Source: UNCTAD based on the United Nations Global Policy Model.
Notes: Output growth is based on GDP at constant 2015 prices (market exchange rates). Grey dashed lines denote average annual growth rates for 2004–2007, 2011–2019 and 2023–2025. Inflation corresponds to a weighted average of national and regional GDP deflators.
a Estimate.
b Projection.

Table I.1
World output growth, 1991–2025

GDP growth rates
(Annual percentage change)

Country groups	1991–1999[a]	2000–2009[a]	2010–2014[a]	2015–2019[a]	2019	2020	2021	2022	2023	2024[b]	2025[b]
World	**2.9**	**3.4**	**3.2**	**3.0**	**2.6**	**-3.0**	**6.3**	**3.1**	**2.7**	**2.7**	**2.7**
▶ Africa	**2.4**	**5.5**	**2.6**	**2.9**	**2.6**	**-2.4**	**4.6**	**3.4**	**3.0**	**3.0**	**3.2**
South Africa	2.7	4.0	2.5	1.0	0.3	-6.0	4.7	1.9	0.6	0.9	1.4
▶ North Africa (incl. South Sudan)	2.7	5.3	-1.9	3.8	2.3	-3.3	4.7	2.6	2.5	2.6	3.2
▶ Sub-Saharan Africa (excl. South Africa and South Sudan)	2.0	6.4	6.2	2.9	3.4	-1.0	4.4	4.3	3.8	3.8	3.6
▶ America	**3.4**	**2.5**	**2.4**	**1.9**	**1.8**	**-3.4**	**6.0**	**2.5**	**2.4**	**2.3**	**2.0**
▶ Latin America and the Caribbean	3.2	3.4	3.4	0.1	-0.6	-7.3	7.1	4.1	2.1	2.0	2.5
Mexico	3.0	1.9	3.2	2.0	-0.4	-8.4	6.0	3.7	3.2	2.0	1.5
▶ Central America (excl. Mexico) and Caribbean	2.8	4.4	3.6	3.0	2.2	-8.7	8.3	4.8	3.6	3.1	3.0
▶ South America	3.4	3.9	3.4	-0.9	-1.1	-6.7	7.3	4.1	1.5	1.8	2.8
Argentina	4.6	3.8	2.7	-0.3	-2.0	-9.9	10.4	5.0	-1.6	-3.5	4.8
Brazil	2.9	3.6	3.2	-0.4	1.2	-3.3	4.8	3.0	2.9	2.8	2.2
▶ Northern America	3.4	2.3	2.1	2.3	2.4	-2.4	5.8	2.1	2.4	2.4	1.8
Canada	2.8	2.3	2.6	2.0	1.9	-5.0	5.3	3.8	1.2	1.1	2.1
United States	3.5	2.3	2.1	2.4	2.5	-2.2	5.8	1.9	2.5	2.5	1.8
▶ Asia (excl. Cyprus)	**4.4**	**5.6**	**5.7**	**4.8**	**3.8**	**-0.9**	**6.7**	**3.6**	**4.2**	**4.0**	**4.0**
▶ Central Asia	-4.4	8.1	6.7	3.7	4.2	-1.2	5.4	4.1	5.6	3.6	3.5
▶ East Asia	4.4	5.6	5.8	4.8	4.0	0.4	6.9	2.5	4.2	3.9	3.7
China	11.0	10.6	8.6	6.8	6.0	2.2	8.4	3.0	5.2	4.9	4.6
Japan	1.2	0.9	1.4	0.9	-0.4	-4.2	2.7	1.2	1.8	0.9	1.0
Republic of Korea	6.8	4.9	3.7	3.1	2.3	-0.7	4.6	2.7	1.4	2.3	2.1
▶ South Asia	4.7	6.3	5.4	6.1	3.7	-3.8	8.1	5.7	6.1	5.7	5.5
India	5.9	7.2	6.6	7.0	4.6	-5.9	9.4	6.5	7.7	6.8	6.3
▶ South-East Asia	5.3	5.5	5.7	5.0	4.4	-3.8	3.6	5.6	3.9	4.5	4.4
Indonesia	4.8	5.2	5.8	5.1	5.0	-2.1	3.7	5.3	5.0	5.1	5.2
▶ Western Asia (excl. Cyprus)	4.3	5.1	5.4	2.9	1.6	-2.9	6.9	6.2	2.0	2.4	3.9
Saudi Arabia	2.2	4.3	5.7	2.2	1.1	-3.6	5.1	7.5	-0.8	1.7	4.7
Türkiye	3.9	5.0	7.6	4.3	0.9	1.7	11.8	5.3	4.5	3.5	3.8
▶ Europe (incl. Cyprus)	**1.4**	**2.2**	**1.2**	**2.1**	**1.8**	**-5.9**	**6.3**	**3.0**	**0.7**	**1.2**	**1.6**
Russian Federation	-5.9	6.2	3.1	1.2	2.2	-2.7	5.9	-1.2	3.6	3.5	1.5
United Kingdom	2.6	2.0	1.8	2.0	1.6	-10.4	8.7	4.3	0.1	0.9	1.4
▶ European Union	1.9	1.8	0.8	2.2	1.8	-5.6	6.1	3.5	0.5	1.0	1.6
▶ Euro area	1.9	1.6	0.6	2.0	1.6	-6.1	6.0	3.5	0.5	0.9	1.4
France	1.8	1.6	1.1	1.7	1.8	-7.5	6.4	2.6	1.1	1.0	1.3
Germany	1.6	1.0	2.0	1.8	1.1	-3.8	3.2	1.8	-0.2	0.2	1.2
Italy	1.4	0.7	-0.8	1.1	0.5	-9.0	8.3	4.0	0.9	0.9	1.0
▶ Oceania	**3.7**	**3.2**	**2.8**	**2.7**	**2.0**	**-2.1**	**5.4**	**3.7**	**1.9**	**1.4**	**2.1**
Australia	3.7	3.3	2.8	2.5	1.8	-2.1	5.5	3.9	2.0	1.4	2.1
▶ Developed countries	**2.3**	**2.2**	**1.7**	**2.1**	**1.9**	**-3.9**	**5.7**	**2.5**	**1.6**	**1.8**	**1.7**
▶ Developing countries	**4.9**	**6.4**	**5.8**	**4.4**	**3.6**	**-1.6**	**7.2**	**3.9**	**4.2**	**4.1**	**4.2**

Sources: UNCTAD based on the United Nations Global Policy Model; United Nations, Department of Economic and Social Affairs, National Accounts Main Aggregates database; United Nations, Department of Economic and Social Affairs, World Economic Situation and Prospects, update as of June 2024; Economic Commission for Latin America and the Caribbean, 2024; Organisation for Economic Co-operation and Development (OECD), 2024; International Monetary Fund (IMF), World Economic Outlook; Economist Intelligence Unit, EIU Country Data database; JP Morgan, Global Data Watch; and national sources.
Notes: The composition of the five geographical regions follows the M49 standard of the United Nations Statistics Division. The distinction between developed and developing countries is based on the updated M49 classification of May 2022. Calculations for country aggregates are based on GDP at constant 2015 dollars.
a Average.
b Forecast.

Given these circumstances, monetary authorities stepped in to stimulate demand through a drastic loosening of monetary policy (UNCTAD, 2013; Palley, 2016). Yet despite negative real interest rates in many economies after the global financial crisis, global growth did not recover to levels necessary to diminish government debt levels sufficiently in relation to GDP (section E).

Twelve years later, as fallout from the COVID-19 pandemic pushed the global economy into another deep recession, the policy response by advanced economies differed substantially from that seen in the aftermath of the global financial crisis. Very low or negative interest rates and the expansion of liquidity in capital markets through quantitative easing allowed Governments to offer relatively cheap fiscal support to households and firms. Particularly in advanced economies, Governments implemented a far more significant budgetary stimulus. By providing massive and temporary income transfers, they attenuated the sudden stop of their economies in 2020 and helped to propel the recovery in 2021.

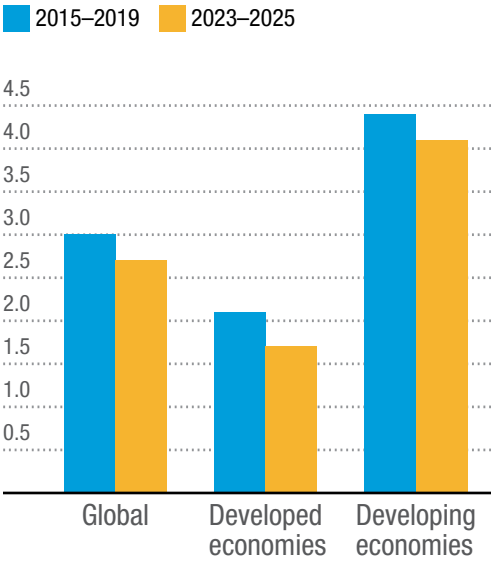
Global output growth is stabilizing at rates below those registered prior to the pandemic.

As proof of the effectiveness of fiscal policy when it is both concerted and of sufficient magnitude, the global economy bounced back strongly in 2021. In a context of tightening fiscal and already very restrictive monetary stances, however, global output growth from 2023 through projections for 2025 shows signs of stabilizing at rates below those registered in the years prior to the pandemic for both developed and developing economies (figure I.2). Even the pre-pandemic global growth trajectory was far from satisfactory, at over a full percentage point lower than before the global financial crisis. Growth was and continues to be insufficient to meet current global development challenges and goals.

Global growth stagnation reflects the trajectories of the world's principal economic regions.

The situation is particularly concerning for the 46 least developed countries. Total output growth for them is expected to average 3.9 per cent annually from 2023 to 2025, a rate woefully short of the "at least 7 per cent annual growth" set for these countries in the Sustainable Development Goals.[1] Only one, Rwanda, is expected to attain this growth rate.

Figure I.2
Economic growth is plateauing at rates below pre-pandemic levels in both developed and developing economies
Real GDP growth rate averages
(Percentage)



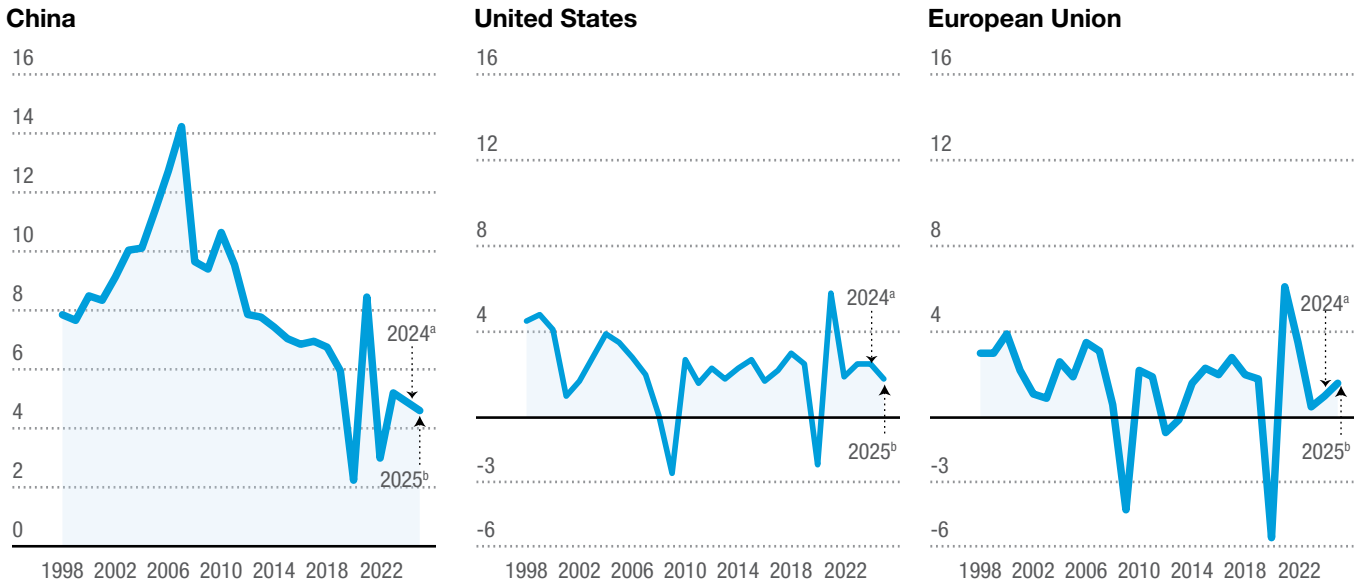
Source: UNCTAD based on the United Nations Global Policy Model.

Note: Output growth is based on GDP at constant 2015 prices (market exchange rates). Data for 2024 are estimates and those for 2025 are projections.

The stagnation in global growth reflects the trajectories of the world's principal economic regions, with ongoing depressed growth in the United States and European Union, and a marked deceleration of the economy of China that began after the global financial crisis (figure I.3). In China, the slowdown partly reflects a reversion to the mean; as the economy grows larger, the same amount of additional real spending results in a lower GDP growth rate. The

[1] See more from the United Nations on Sustainable Development Goal 8, on decent work and economic growth, available at https://www.un.org/sustainabledevelopment/economic-growth/.

Figure I.3
Stagnation and deceleration afflict the world's major economies
Real GDP growth, selected economies
(Percentage)



Source: UNCTAD based on the United Nations Global Policy Model.
Note: Based on GDP at constant 2015 prices.
a Estimate.
b Projection.

deceleration, however, also results from the exhaustion of the construction boom, in both infrastructure and housing, which had substituted for net exports as the main driver of growth in China during the last decade.

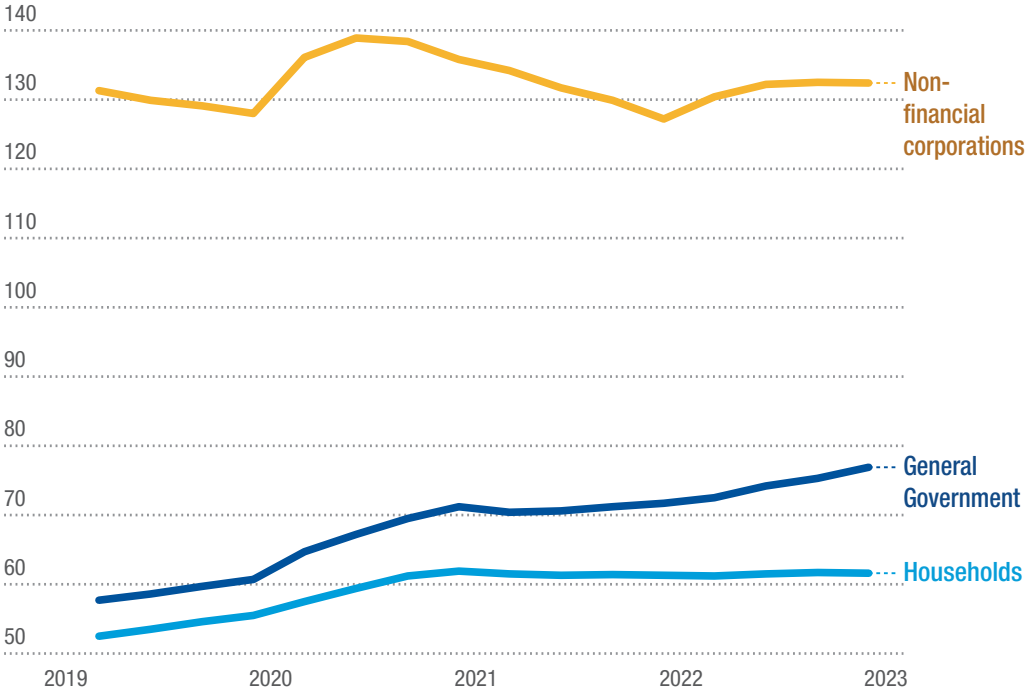
Looking forward, it is unlikely that the main drivers of growth in China over the last two decades – the export sector and a debt-financed construction boom – will continue to provide the same economic impetus. The relatively high (by local standards) debt-to-GDP ratio of Chinese families (at 62 per cent), along with the increasing leverage of non-financial corporations after the Evergrande Group adjustment of 2021–2022 and the continuous growth in the public debt ratio since the outbreak of COVID-19 (figure I.4), suggest that current financial conditions are not conducive for a debt-led domestic construction boom that could act as the main growth driver of the economy. Although net exports have accelerated recently, there is nevertheless heightened uncertainty around the viability of another export-led boom. On the international side, the price policy of Chinese firms has prompted anti-dumping measures in many economies (Friedberg, 2024). On the domestic side, despite rising export quantities, Chinese firms have not registered high profits and are, instead, increasing their debt levels.

The strategy of the Government of China points towards deceleration in GDP growth as the current expansion of investment in innovation, science and technology does not have the same demand effect as previous development phases galvanized by net exports and construction. Rising investments in research and development and science, technology, engineering and mathematics tend to raise productivity and will help to keep China at the forefront of many technologies. But they also mark the beginning of a period of more moderate growth in the absence of government policies to raise domestic private and public consumption.

Figure I.4

The upward trajectory in public and corporate debt in China resumed from early 2022 onwards

Credit-to-GDP ratios of non-financial corporations, General Government and households in China
(Percentage)



Source: UNCTAD based on the Bank for International Settlements.
Notes: Households include non-profit institutions serving households. General Government refers to central, State and local governments and the social security funds controlled by these bodies.

In terms of the global economy, its near paralysis in 2020 and bounce back in 2021 created numerous supply bottlenecks, with significant but temporary inflationary pressures in global value chains (UNCTAD, 2023b; Stiglitz, 2023). These supply pressures were exacerbated by transitory shifts in consumption patterns towards durable goods (UNCTAD, 2022) as well as a surge in commodity prices (chapter II). Monetary authorities across the financially advanced economies reacted to the uptick in inflation with a sharp increase in policy rates that saw real interest rates move back to positive values in these countries (chapter I, section D).

The acceleration of prices has proven to be chiefly a supply issue.

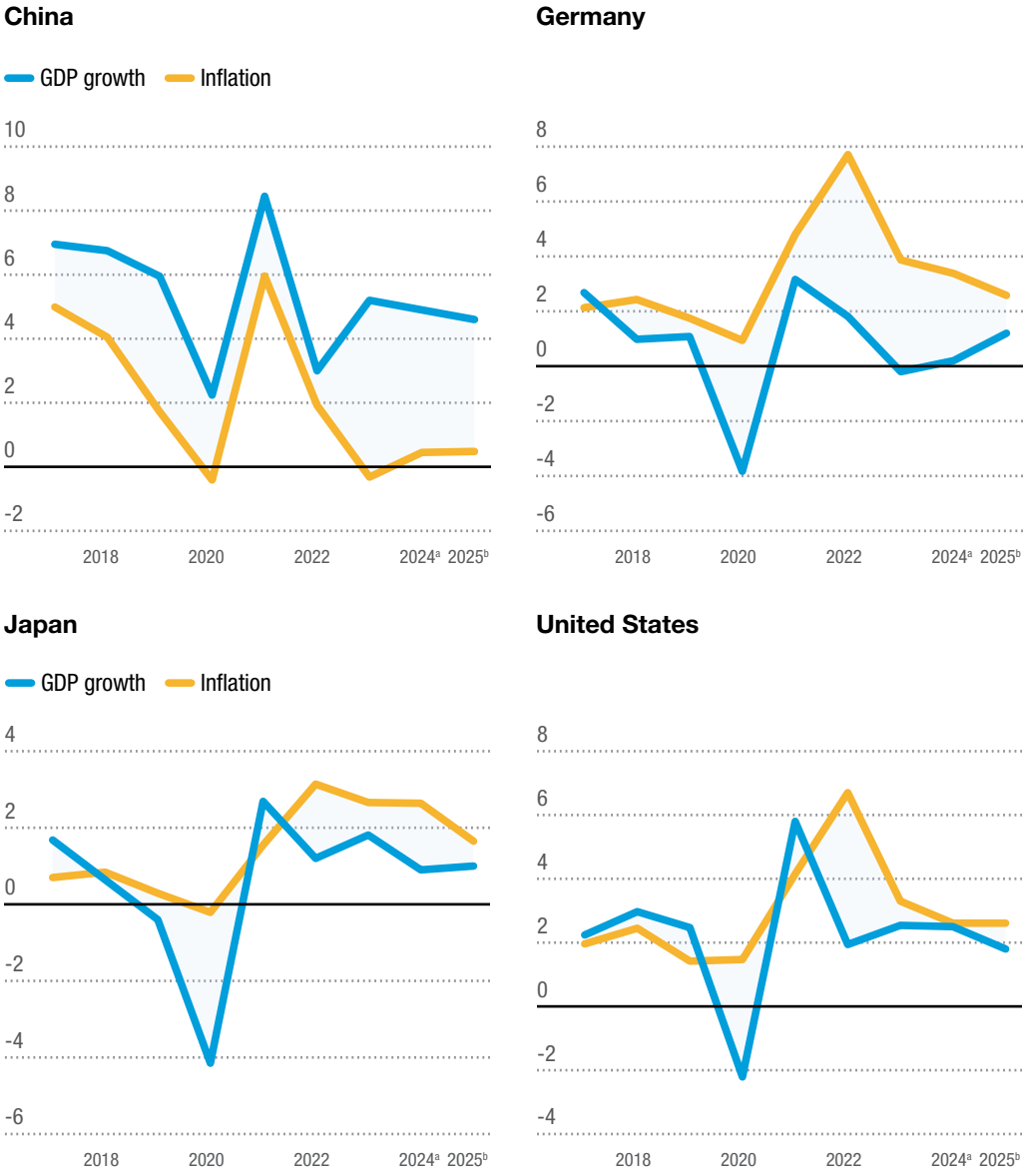
Nearly five years after the pandemic, monetarist worries about a "great post-pandemic inflation" seem misplaced. The acceleration in prices has proven to be chiefly a supply issue – a sellers' instead of a buyers' inflation. Along with other contributing factors, firms adapted to structural changes in relative prices and used their market power to transfer cost increases to consumers (UNCTAD, 2023b; Weber and Wasner, 2023). As of mid-2024, the upward trajectory in prices has slowed across the globe. This disinflationary process is taking place amid significantly diverging growth trajectories, however, including among the economies of the Group of 20 (chapter I, section G).

In numbers, the United States is set for a relatively soft landing in 2024 as the economy settles on a 2 per cent growth trend. China continues to decelerate to a still uncertain trend growth rate. Japan seems to be on the path to a stable 1 per cent growth rate, while Germany continues to struggle to reach the same, fairly meagre 1 per cent rate after being hit hard by the twin shocks of the pandemic and the war in Ukraine (figure I.5).

Figure I.5

Economic growth rates have diverged among the largest countries

Real GDP growth and inflation, selected countries of the Group of 20
(Percentage)



Source: UNCTAD based on the United Nations Global Policy Model.
Notes: Output growth is based on GDP at constant 2015 prices. Inflation corresponds to the GDP deflator.
a Estimate.
b Projection.

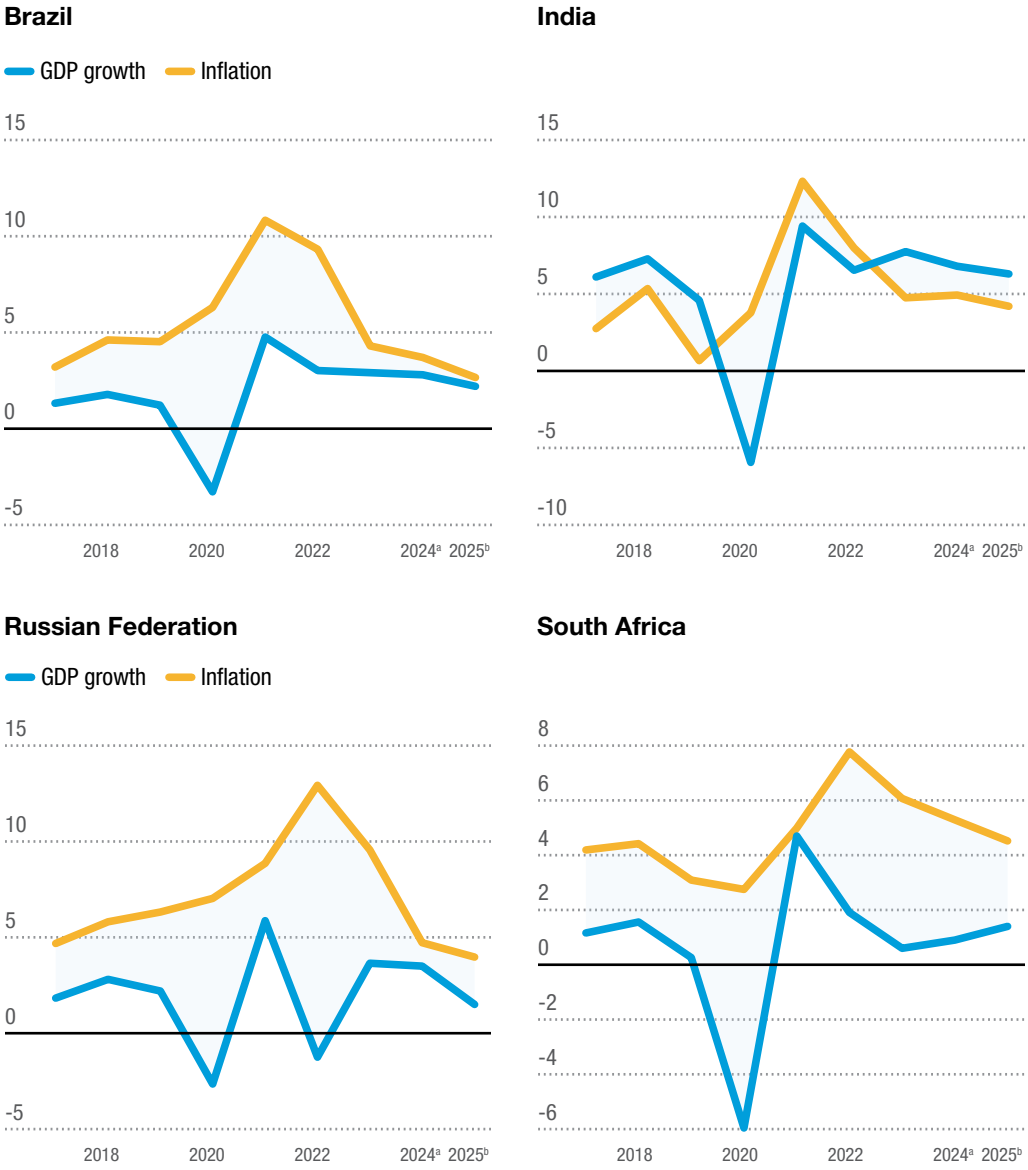
The economies of Brazil, the Russian Federation, India, China and South Africa (BRICS), apart from China, also saw a post-pandemic spike in inflation but with very different growth and price trajectories (figure I.6). Specifically, after a decade of stagnation, Brazil seems to be converging to a 2 per cent growth rate and a 3 per cent inflation rate. In contrast, the economy of the Russian Federation appears to be converging to a 4 per cent inflation rate. Much uncertainty persists regarding its

GDP growth due to a "W" growth pattern caused by shocks from the COVID-19 pandemic and the impact of the war in Ukraine on Russian trade and investment. The GDP growth of India appears stable at 6 per cent, with an accompanying inflation rate of 4 per cent, while South Africa is struggling to reach a 2 per cent growth rate and a 4 per cent inflation rate by 2025.

Figure I.6

Diverging growth and inflation trajectories prevail among BRICS economies (excluding China)

Real GDP growth and inflation
(Percentage)



Source: UNCTAD based on the United Nations Global Policy Model.
Notes: Output growth is based on GDP at constant 2015 prices. Inflation corresponds to the GDP deflator.
a Estimate.
b Projection.

C. The macroeconomics of consumer discontent

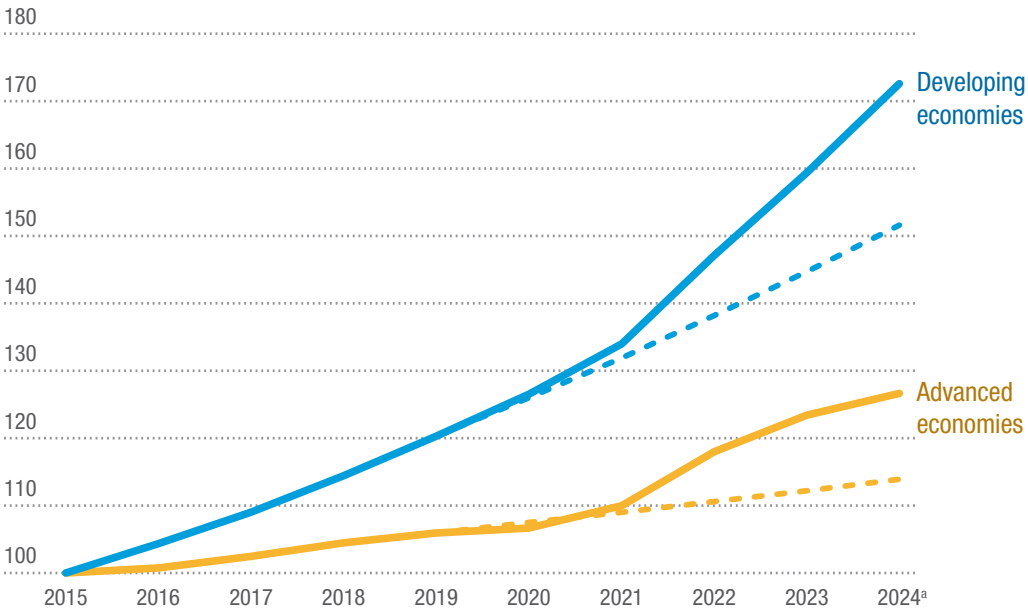
The post-COVID-19 recovery and disinflation have been accompanied by widespread discontent across countries. The sharp increase in the cost of credit – a result of hiking interest rates – has hit households particularly hard amid high household debt levels. Consequently, far too many households have had to cut spending as their disposable income shrinks. Similarly, the trajectory of consumer prices, which despite the disinflation of recent years has not returned to its pre-pandemic trend, has significantly eroded household purchasing power. Consumer prices are 11 and 14 per cent higher for advanced and developing countries, respectively, than the levels indicated by the pre-pandemic trend (figure I.7).

Higher prices and credit costs are eating into household disposable income.

Figure I.7

The uptick in consumer prices has eroded household purchasing power in both advanced and developing countries

Consumer price index
(2015=100)



Source: UNCTAD based on data from the IMF World Economic Outlook, April 2024.
Notes: Dashed lines correspond to estimates based on the pre-pandemic trend (2015–2019). Aggregations for advanced and developing economies are computed using geometric means.
a Estimate.

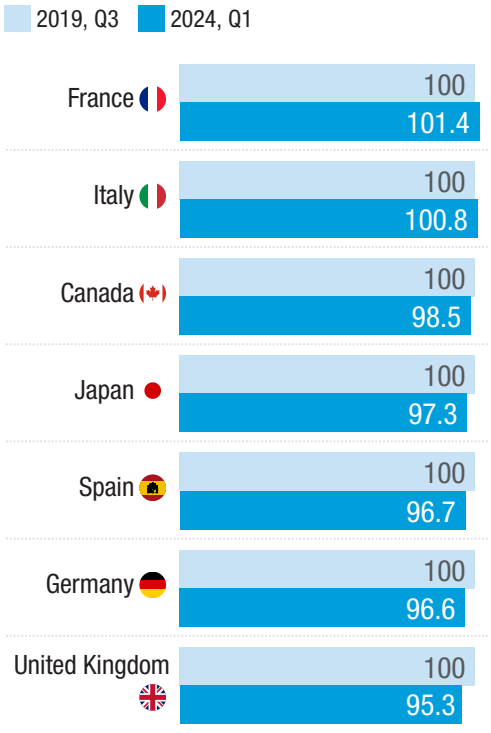
Real spending by households in many countries is still below pre-pandemic levels.

These price dynamics and the accompanying reduction in consumer purchasing power have, in some countries, led to a stagnation and, in others – particularly where fiscal support for households during the pandemic was more restrained – a decline in household per capita real consumption spending relative to before the pandemic (figure I.8).

Figure I.8

Consumption spending by households in numerous countries has yet to recover to its pre-pandemic level

Real final consumption expenditure per capita of households, selected OECD countries
(Third quarter of 2019=100)



Source: UNCTAD based on OECD database.
Abbreviations: Q1, first quarter; Q3, third quarter.

The post-pandemic spike in inflation was the product of a combination of factors.

A key feature of economic activity in the post-pandemic period concerns policy responses to the uptick in inflation that began in 2021. As outlined by UNCTAD in recent editions of the Trade and Development Report, the post-pandemic spike in inflation was not simply a result of overheating economies in which too much money was chasing too few goods and services. It was instead the product of a combination of factors, including transitory supply bottlenecks, shifting consumption patterns, surging commodity prices, heightened market concentration and the pricing behaviour of large corporations in certain sectors, most notably agrifood and energy (UNCTAD, 2023b).

The structure of inflation – with many supply-side issues unresolved to this day – raises questions about the efficacy of the monetary stance. Excessive reliance on sharp and prolonged monetary tightening as the sole policy tool to bring inflation down to target rates in the major advanced economies is destined to be only partially effective, just as the loosening of monetary policy in the deflationary period after the global financial crisis was unable to push inflation up to target rates. At the same time, monetary tightening has been costly as a major factor in restricting economic activity; increasing financing costs for households, firms and Governments; exacerbating financial instability risks; adding pressure on currencies; and amplifying debt burdens across developing countries (UNCTAD, 2024c). A more balanced policy mix that addresses the different forces driving inflationary pressures would be more effective and entail less “collateral damage”.

Such a mix would include concerted actions to rein in anti-competitive practices, abuses of dominant market positions and corporate concentration in key sectors. It would comprise price stabilization tools and revisions to the existing regulatory framework for commodity-trading activities to curb excessive financial speculation, and put a stronger focus in monetary policy on financial stability and liquidity management in the financial system (UNCTAD, 2020, 2023).

D. Delayed monetary loosening and a strengthening dollar

Discussions among economists before the pandemic on whether the global economy had entered an era of secular stagnation appear to have been settled by the COVID-19 shock. Proponents of secular stagnation had insisted that subdued growth trends after the global financial crisis were a by-product of diminished investment levels despite historically low interest rates – due to increases in the savings rate – that brought about a persistent shortfall in aggregate demand. In fact, the negative real interest rates of the 2010s resulted from an insufficient fiscal impulse to offset the fall in private sector fixed capital investment after the financial crisis (UNCTAD, 2015; Cooper, 2022).

The combination of supply bottlenecks and a series of other factors during and after the pandemic created a temporary inflationary spike worldwide, igniting an almost synchronized increase in interest rates in the major advanced economies (figure I.9). Policy rates in the United Kingdom and United States as well as the euro area jumped sharply from late 2021 through the middle of 2023. Despite expectations at the beginning of 2024 that monetary loosening cycles would begin shortly and would by now be well under way, there have been repeated delays to the much-anticipated start of the loosening cycle.

After numerous postponements, the European Central Bank finally began its process of monetary loosening with a 25-basis-point reduction in its key interest rates on 6 June 2024. A further 25-basis-point cut to its deposit rate occurred on 12 September. Interest rate cuts in the United Kingdom and United States were pushed back to the second half of 2024, with the Bank of England reducing its bank rate by 25 basis points on 16 August and the Federal Reserve System lowering its federal funds target rate by 50 basis points on 18 September. Despite these initial steps towards monetary loosening, the cumulative magnitude of rate increases from 2021 to 2023 has resulted in monetary stances that remain highly restrictive.

The increase in policy rates in the major advanced economies was replicated throughout much of the developing world (figure I.9). In the case of these countries, the pace of monetary normalization will inevitably diverge somewhat based on differing inflationary and exchange-rate trajectories as well as other specific domestic factors at play in each country. In Latin America, Brazil and Chile were the first to hike interest rates, followed by Colombia and Mexico. As of mid-2024, the Brazilian situation is uncertain, with possible new hikes in 2025, whereas Mexico has yet to start its monetary easing. In Chile and Colombia, central banks are expected to continue cutting rates gradually.

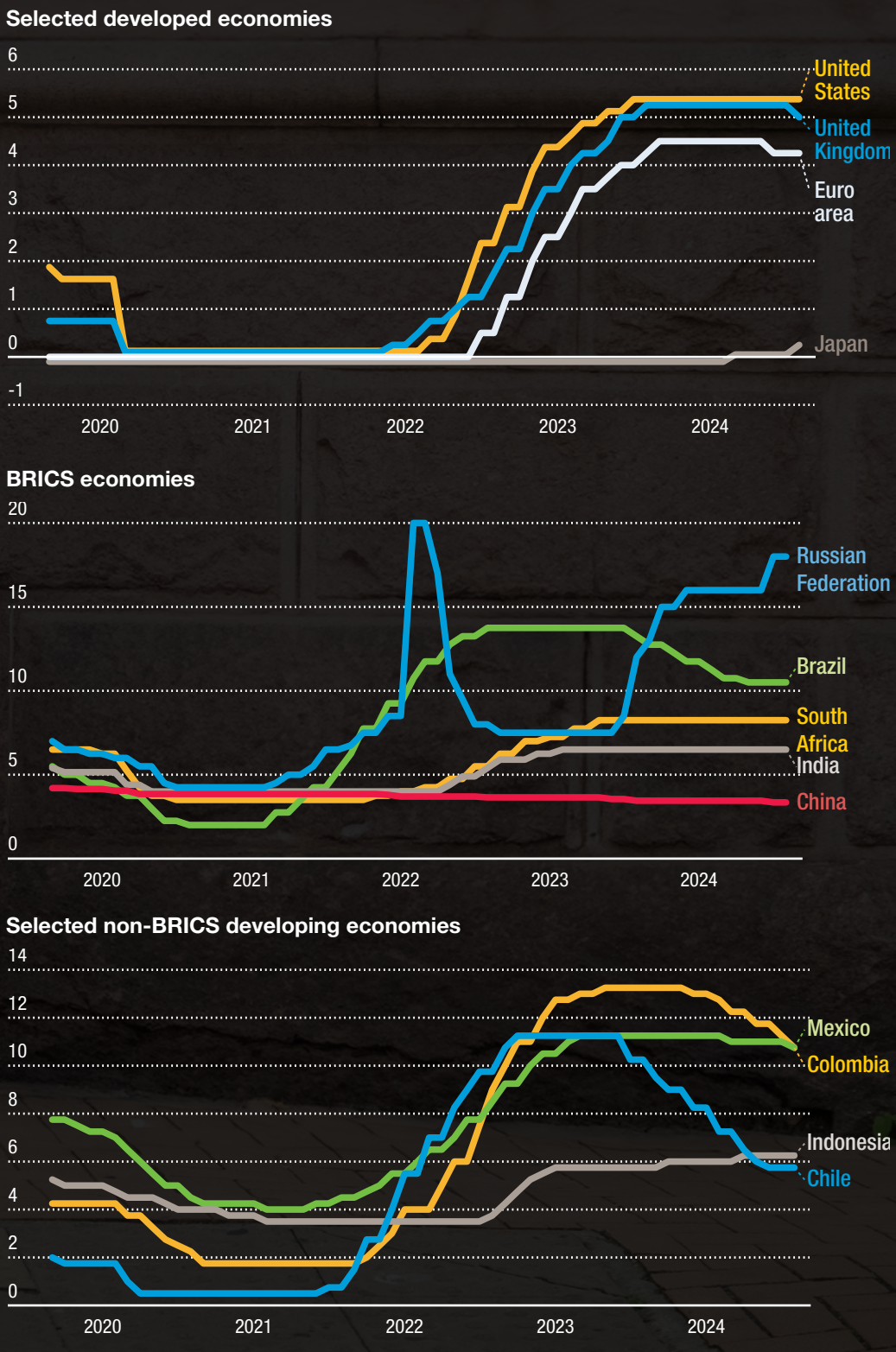
There have been repeated delays to the much-anticipated start of monetary loosening.

India, Indonesia and South Africa are still in the high nominal rate phase, with no significant cuts predicted for 2024–2025. China continues its gradual monetary easing, with the possibility of further cuts in 2024–2025 to avoid a deceleration in economic growth. In the Russian Federation, the central bank is expected

Figure I.9

Monetary policy rates remain high across the globe

Central bank policy (short-term) interest rates
(Percentage)



Source: Bank for International Settlements.

to maintain its high interest rate to deal with ongoing exchange rate and price pressures imposed by the war in Ukraine.

Along with specific domestic factors in each country, the delay in monetary loosening in major developed economies is a key factor in exerting pressure on central banks across developing countries. As a result, these banks see the need to maintain a tighter monetary policy than would otherwise be necessary to avoid interest rate differentials that might stoke capital outflows and domestic currency depreciations. At the same time, the ending of quantitative easing raises new challenges in rolling over foreign currency bonds issued by developing country Governments during the period when key central banks had facilitated the issuance of such bonds through their quantitative easing programmes.

The main monetary novelty so far in 2024 has happened in Japan, where the Bank of Japan ended its almost eight-year negative nominal interest rate. The Japanese policy interest rate is still close to zero, and the real interest rate is negative, but the recent 20-basis-point change in the short-term carry trade that uses the yen as the borrowing counterpart is expected to attenuate the sharp post-pandemic depreciation of the Japanese currency against other main reserve currencies (figure I.10).

Outside Japan, the currencies of other major advanced economies have registered a gradual appreciation over 2024 (figure I.10). In developing economies, despite tight stances adopted by monetary authorities, most have seen a depreciation of their currencies vis-à-vis the dollar. Out of 94 developing economies that operate under non-fixed exchange rate regimes and for which data are available,[2] 79 registered a nominal depreciation in the first half of 2024.

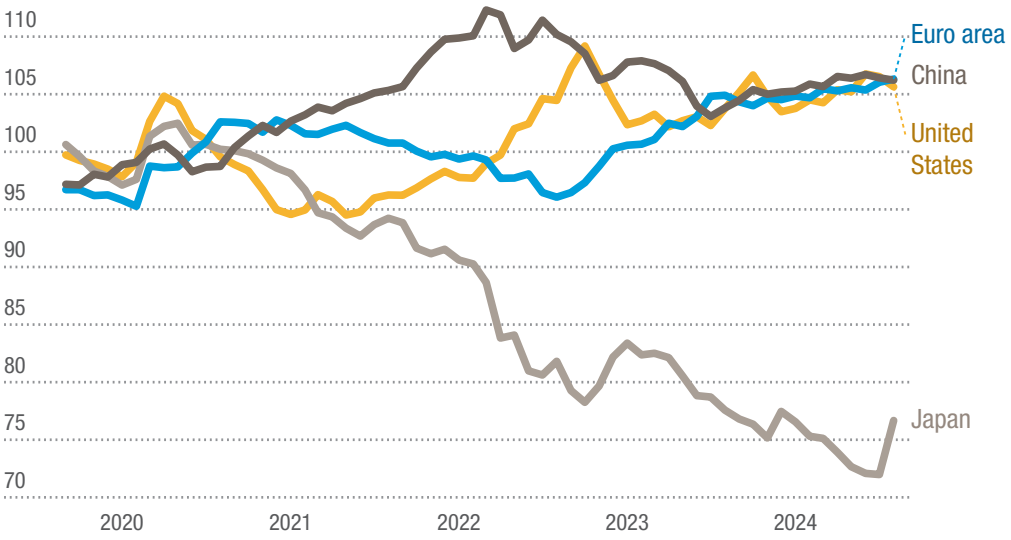
Delays in monetary loosening in developed economies have exerted pressure on central banks across the global South.

Of 94 developing economies under non-fixed exchange-rate regimes, 79 registered a depreciation against the dollar in 2024.

Figure I.10

Except for the yen, main reserve currencies are registering a gradual appreciation in 2024

Effective nominal exchange rate index
(2020=100)



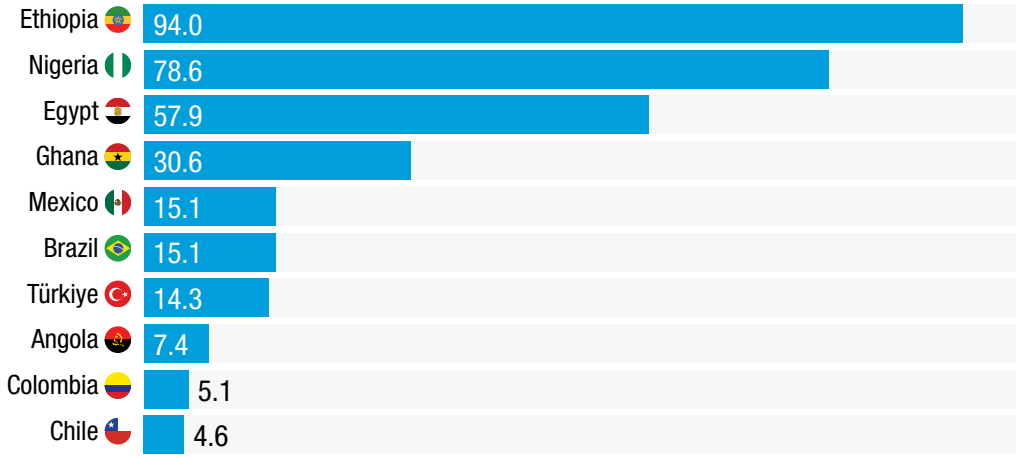
Source: Bank for International Settlements.
Note: Nominal effective exchange rates are calculated as geometric trade-weighted averages of bilateral exchange rates.

[2] See the BIS Data Portal on bilateral exchange rates, available at https://data.bis.org/topics/XRU/data.

Figure I.11

Several developing economies have suffered sharp depreciations of their currencies in 2024

Bilateral exchange rate depreciations relative to the United States dollar in nominal terms, selected developing countries, January–August 2024
(Percentage)



Source: UNCTAD based on London Stock Exchange Group Eikon.
Note: Percentage change in the nominal exchange rate against the United States dollar between 1 January 2024 and 22 August 2024.

Ongoing tight international monetary conditions have put additional pressure on developing country currencies.

Some have experienced particularly severe drops (figure I.11) that are fuelling inflationary pressures in their economies. While specific domestic factors are also at play (section G), particularly in countries undergoing very sharp depreciations, ongoing tight international monetary conditions have exacerbated pressures on local currencies across the developing world.

The combination of continuing high policy rates in major advanced economies and depreciating domestic currencies is severely limiting the policy space available to authorities in developing countries. It is also increasing the servicing costs of foreign currency-denominated debt. This situation is squeezing fiscal accounts and heightening potential risks to financial stability.

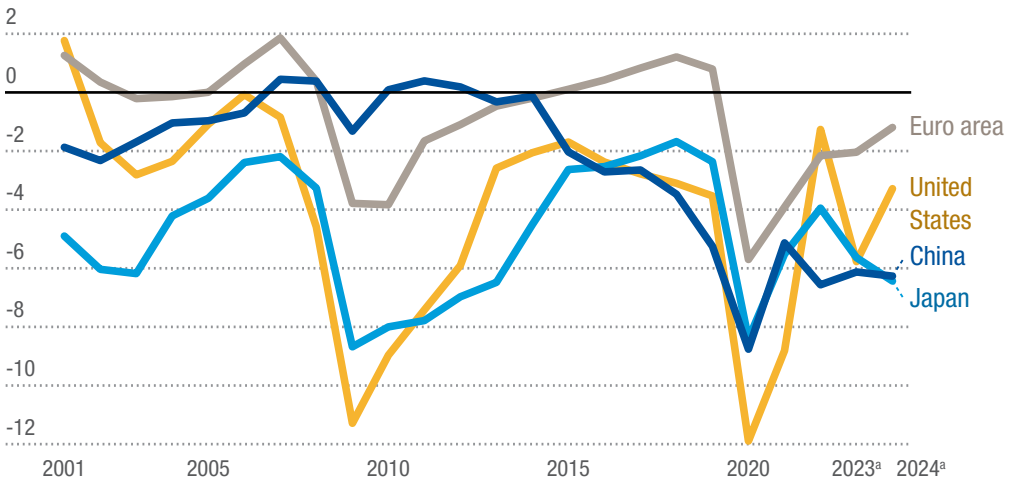
E. The phasing out of fiscal stimulus and increased public debt levels

The largest economies of the Group of 20 responded to the COVID-19 shock with fiscal stimuli of very different sizes. In the United States, the primary balance fell from a deficit of 3.5 per cent of GDP in 2019 to almost 12 per cent of GDP in 2020. The fiscal consolidation taking place since then is expected to bring fiscal accounts back to a primary deficit of 4 per cent of GDP in 2024. Comparing the response in the United States to the global financial crisis and the COVID-19 shock, the fiscal impulse or change in the primary deficit was more significant in 2020 than in 2009 (figure I.12).

The euro area's fiscal response to the global financial crisis and the COVID-19 shock was also a stimulus but of a smaller magnitude and with a faster budgetary consolidation than in the United States. In recent years, the primary balance has fallen from a surplus of 0.7 per cent of GDP in 2019 to a deficit of approximately 6 per cent in 2020. Fiscal consolidation started in 2021 and is expected to bring the euro area to a deficit of roughly 1 per cent of GDP in 2024.

In Asia, Japan responded to both the global financial crisis and COVID-19 shock with a similar fiscal impulse, a 5-percentage-point increase in the ratio of the primary deficit to

Figure I.12
Diverging fiscal balance dynamics among the world's largest economies
Primary fiscal balance in selected economies of the Group of 20
(Percentage of GDP)



Source: IMF World Economic Outlook, April 2024.
a Estimate.

The COVID-19 shock raised public debt in almost all economies of the Group of 20.

GDP. In contrast, China became much more fiscally active after the pandemic compared to the global financial crisis. In 2009, China had a temporary and small primary deficit, followed by an almost balanced primary budget in 2010–2014. The situation started to change in 2015, when the primary deficit started to increase. By 2019, the deficit had reached 5 per cent of GDP; the COVID-19 shock saw it deepen to almost 9 per cent of GDP in 2020. For 2024–2025, the expectation is for the primary deficit to stabilize at approximately 6 per cent of GDP. As outlined below, increases in primary deficits are reflected in the swelling of public debt stocks.

As expected after a recession, the COVID-19 shock raised public debt in almost all Group of 20 economies (table I.2). The exceptions were Brazil and Türkiye, for

Table I.2

Public debt levels spiked in the aftermath of the COVID-19 shock

General government gross debt in the economies of the Group of 20
(Percentage of GDP)

Country	COVID-19 shock period					Change
	2019	2020	2021	2022	2023[a]	2019–2023
Argentina	90	104	81	85	155	65
Australia	47	57	56	50	49	3
Brazil	87	96	89	84	85	-2
Canada	90	118	114	107	107	17
China	60	70	72	77	84	23
Euro area	84	97	95	91	89	5
France	97	115	113	112	111	13
Germany	60	69	69	66	64	5
Italy	134	155	147	141	137	3
India	75	88	84	82	83	8
Indonesia	31	40	41	40	40	9
Japan	236	258	254	257	252	16
Mexico	52	59	57	54	53	1
Republic of Korea	42	49	51	54	55	13
Russian Federation	14	19	16	19	20	6
Saudi Arabia	22	31	29	24	26	5
South Africa	56	69	69	71	74	18
Türkiye	32	39	40	31	29	-4
United Kingdom	86	106	105	100	101	15
United States	108	132	125	120	122	14

Source: IMF World Economic Outlook, April 2024.
a Estimate.

idiosyncratic reasons. In Brazil, there was already a large public debt build-up before the crisis, and the Government was in the middle of fiscal restructuring when the pandemic hit. In Türkiye, high inflation, fast growth and low real interest rates attenuated the impact of the COVID-19 shock on debt dynamics.

In the remaining Group of 20 countries, the most significant debt expansion happened in Argentina, mostly in 2023, due to the maxi-depreciation of the peso that year. Since most government debt is indexed to the United States dollar, the Argentine stabilization strategy had an outsized negative impact on fiscal solvency. The second largest public debt build-up was registered in China (up 23 percentage points of GDP) but it had a relatively low debt ratio before the pandemic. In most of the largest advanced economies, the pandemic increased gross public debt by about 13 to 17 percentage points of GDP. In the remaining developing economies, the most significant debt increase happened in South Africa, with a rise of 18 percentage points of GDP.

The burden of increased debt levels in terms of the quantity of public resources that have to be dedicated to servicing these liabilities is further aggravated by tight international financial conditions (chapter II) and depreciating currencies. A greater proportion of public funds have to be channelled to debt servicing instead of much needed public services and investments in areas key to achieving development and climate goals.

While some proponents of fiscal consolidation point to increased deficits and public debt stocks as evidence of the need for Governments to restrict spending, this policy prescription does nothing to address shortfalls in needed public outlays to tackle development challenges facing developing economies. In fact, it worsens these challenges. Addressing the adverse effects of fiscal imbalances and resulting debt dynamics while simultaneously maintaining sufficient public investment in closing developmental gaps requires a far more proactive response.

On the fiscal side, a key factor in responding to fiscal imbalances and heightened government debt liabilities entails making sure that fiscal revenues adequately reflect the economic and financial gains reaped by larger corporations and top earners. Corporations use myriad tools to avoid tax obligations,[3] draining public coffers and severely hindering government capacities to mobilize resources for essential public services and investments (UNCTAD, 2017). Progress in redressing these practices requires a coordinated clamping down on corporate arbitrage practices, tax havens and conduit jurisdictions, but also a multilateral mechanism that can enable developing countries to reverse asymmetries in negotiating positions over double taxation agreements (chapter V).

Greater access to affordable, reliable and longer-term financing options – particularly for the most vulnerable developing countries – is another key factor in ensuring adequate public outlays towards development goals. Important policy actions on the international sphere include increased concessional finance through the capitalization of multilateral and regional banks, the issuance of new and the reallocation of existing special drawing rights, the use of innovative financial instruments (e.g. sustainable development bonds and resilience bonds), and the expansion of currency swap facilities, pioneered by the Federal Reserve, to facilitate borrowing in domestic currency over foreign currency (UNCTAD, 2023b).

On the monetary side, rather than focusing exclusively on inflation targets in determining policy, monetary authorities – particularly those in major advanced economies – should consider the wider impacts of their

A clamping down on tax avoidance by corporations and a multilateral mechanism to strengthen negotiating positions of developing countries are needed.

[3] The most important of these tax-planning tools entail shifting profits to affiliates located in tax havens, shifting liabilities to affiliates located in high-tax jurisdictions, transfer pricing through deliberately inaccurate valuations of intra-firm cross-border transactions, and exploiting tax loopholes in domestic tax laws and international tax treaties (UNCTAD, 2020).

Monetary authorities should consider the wider impacts of their decisions.

decisions. Factors to deliberate include the impacts of monetary decisions on debt trajectories and servicing costs, the financing of critically needed investments, financial sustainability and gaps in capital provision (UNCTAD, 2023b, box I.2).

Changes in the criteria and functioning of policymaking cannot be ad hoc. They need to be embedded in the mandates of monetary institutions. The quantitative easing response to the global financial crisis demonstrated that monetary policy is most effective when used for financial stabilization rather than simply for regulating inflation and the business cycle, where the lags and uncertain functioning of monetary transmission mechanisms weaken policy effectiveness.

Box I.1
Pleasant and unpleasant fiscal arithmetic

The rise in public debt after the COVID-19 shock raised the usual concerns about government solvency worldwide, with different calls for action depending on the economy under analysis. In developing economies, there have been recommendations for fast fiscal consolidation to gain policy credibility, even if that requires a significant slowdown or even contraction in GDP at the beginning of the cycle. In contrast, advanced economies have adopted a more gradualistic approach, tolerating higher primary deficits for a more extended period of time, as well as lengthening the time horizon necessary to converge to their inflation targets in order to avoid a spike in real interest rates (Taylor and Barbosa-Filho, 2021).

Theoretically, proper policy coordination and international support could end the double fiscal and monetary standard between advanced and developing economies, allowing developing economies to adopt the same gradualistic adjustment under way in high-income economies. In practice, the challenge lies in reducing the cost of public debt in developing countries, what economists call the "r minus g", the difference between the real interest rate on government bonds (r) and a country's GDP growth rate (g).

Advanced economies can grow out of high debt ratios through moderate primary budget deficits.

Recent research has shown that, in the long run, the real interest rate is lower than GDP growth in advanced economies (Mehrotra and Sergeyev, 2021), creating a pleasant fiscal arithmetic: a country can grow out of high debt ratios through moderate primary budget deficits. In most developing and some advanced economies, by contrast, the "r minus g" is highly positive. This results in an unpleasant fiscal arithmetic for these countries as it necessitates large primary surpluses to keep public debt under control. Since developing countries also need more public spending on universal public services and infrastructure, the current fiscal constraint is incompatible with progress towards the Sustainable Development Goals.

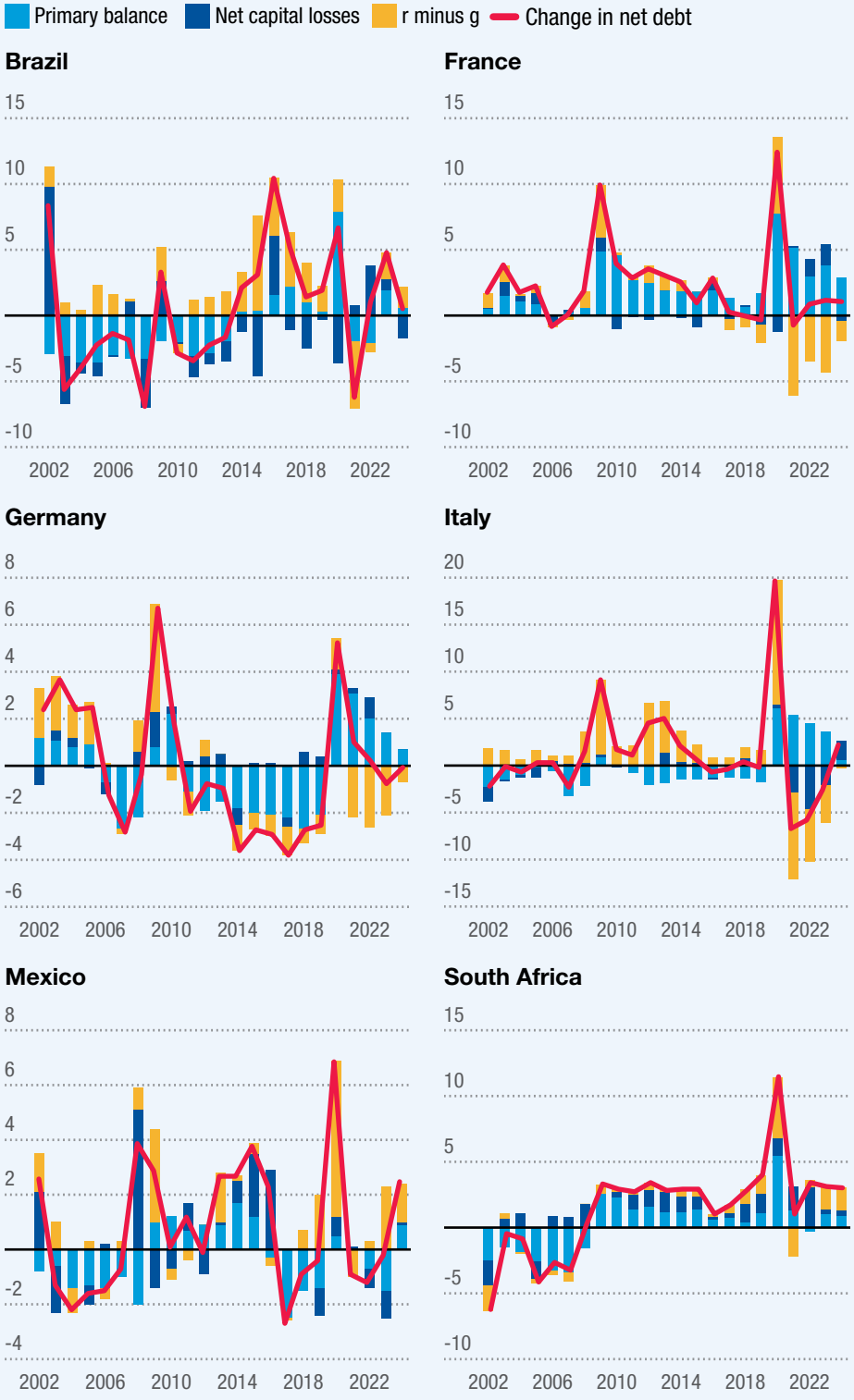
For developing countries, current fiscal constraints are incompatible with progress on sustainable development.

In addition to domestic actions, developing countries' unpleasant fiscal arithmetic requires at least two global responses. The first entails a coordinated increase in taxation on cross-border activities, especially on high net worth individuals and large corporations, to raise government primary balances (Ocampo, 2014). The second involves a multilateral initiative to reduce the risk premia on selected government investments in developing countries, with the IMF and similar institutions acting as a hedge of last resort for the exchange-rate risk from global shocks.

Box I.1 Pleasant and unpleasant fiscal arithmetic

The real interest rate plays a key role in driving debt dynamics

Sources of the change in the net debt-to-GDP ratio, selected economies
(Percentage of GDP)



Source: IMF World Economic Outlook, April 2024.
Notes: The formula "r minus g" is the difference between the real interest rate on government bonds (r) and the country's GDP growth rate (g). Data for 2023 and 2024 are estimates.

Box I.2
Closing the capital gap: The State and central banking

Gaps in the provision of long-term finance become prominent in times of economic difficulties.

Capital markets offer opportunities to end the undue reliance on short-term bank financing, allowing businesses not only to fix financing costs and economize on cash flow but also to get through longer periods of losses before returns on investments in capital equipment start to come in. At the same time, stock markets allow buyers of stocks to provide capital needed by industry in the "primary" market for stocks and shares without having to commit to holding the stocks until the company repays its investors. Stocks can be sold in a "secondary" market to some other financial investor willing to hold them.

Yet the offer of long-term finance is by no means comprehensive. Gaps in provision illustrate how reliance on such finance is far from efficient when it comes to social and economic development. Gaps in capital market provision become especially prominent in times of economic difficulties, when Governments and businesses find themselves financially constrained, or when they face a pressing need such as climate change investments where cash flow benefits are incalculable.

During the Great Depression of the 1930s, in an effort to revive their economies, Governments took over capital market functions and made them available to corporations on the condition that they participated in State-sponsored infrastructure and other investments that were also supported by central banks. This entry of Governments and central banks into investment banking was not an embrace of Keynes's "socialization of investment" (Keynes, 1936). It came about as a result of the failure of capital market functions in the economy. Corporations in industrialized countries found themselves unable to "fund" their balance sheets with stocks and bonds. It was this breakdown, rather than any politically motivated consensus, that laid the foundation for industrial policy and planning after the Second World War (Engerman, 2015).

The flaw in short-term bank finance is the possibility that banks will not roll over borrowing or will only do so at a higher rate of interest. Long-term finance is the obvious solution. But such finance comes with its own distinctive limitations: the narrow scope of its availability and, as demonstrated in successive collapses in stock market trading, the possible illiquidity of stockholders, leading to capital market failure.

In developing countries, most economists have argued that, in a global economy dominated by the first industrial powers, the State needs to take the lead on industrial policy in order to industrialize. But given central bank mandates for managing government debts and monetary policy, it is considered inappropriate for a central bank to manage industrial projects directly. In many developing countries and emerging markets, special purpose "development banks" therefore provide long-term finance for industrial projects. These may have favourable refinancing terms at the central bank to allow them to finance projects over long periods of time without regard to the liquidity of stockholders.

Such a model seems highly appropriate for building infrastructure and developing industry and construction (such as housing). Where the benefit is a common good, such as the green transition, it can provide finance for projects that work rather than using projects for financial (funding) purposes.

The consensus among monetary economists framing central bank operations is that countries at all stages of economic development should apply inflation-targeting, using a short-term policy rate of interest to regulate the inflation rate. There is a disconnect here, however, between the use of an interest rate instrument affecting

Box I.2 Closing the capital gap: The State and central banking

principally banking and short-term credit flows and the capital market through which monetary policy transmission is supposed to work (Toporowski, 2024).

Financial crises in the financially advanced countries, notably after the global financial crisis in the United States and most recently the COVID 19 pandemic, have tempered inflation targeting with considerations of financial stability to provide liquidity assistance to capital markets. But central banks have not, in general, sought to fill gaps in capital market provision for productive investment, innovation and the green transition (UNCTAD, 2023b).

Central banks have not sought to fill gaps in capital market provision.

While there are good reasons for keeping such provision off the balance sheets of central banks, this does not mean that central banks cannot support agencies that can fill gaps in capital markets. Such gaps should not also become holes in central bank policy frameworks.

F. Income inequality on the rise

UNCTAD has maintained that the increase in the labour share of income during the pandemic was a temporary phenomenon due to the relatively larger fall in profits compared to wages and the exclusion of low-wage workers from statistics during lockdowns. Data on the post-pandemic period confirm these expectations.

Using the United Nations Global Policy Model to simulate the evolution of functional income distribution – or the distribution of value added among wages, profits, rents and taxes – in the Group of 20 countries indicates that the labour share of income is continuing to fall in most advanced economies but with divergent real-wage trajectories. In Canada, Germany, the United Kingdom and the United States, the labour share tends to fall in parallel to an increase in the real wage. In Australia, France, Italy and Japan, the labour share has fallen with a stagnant or declining real wage (figure I.13). The combination of declines in the labour share and real wages is particularly troublesome as it points to structural and conjunctural pressures leaving workers increasingly worse off in these countries.

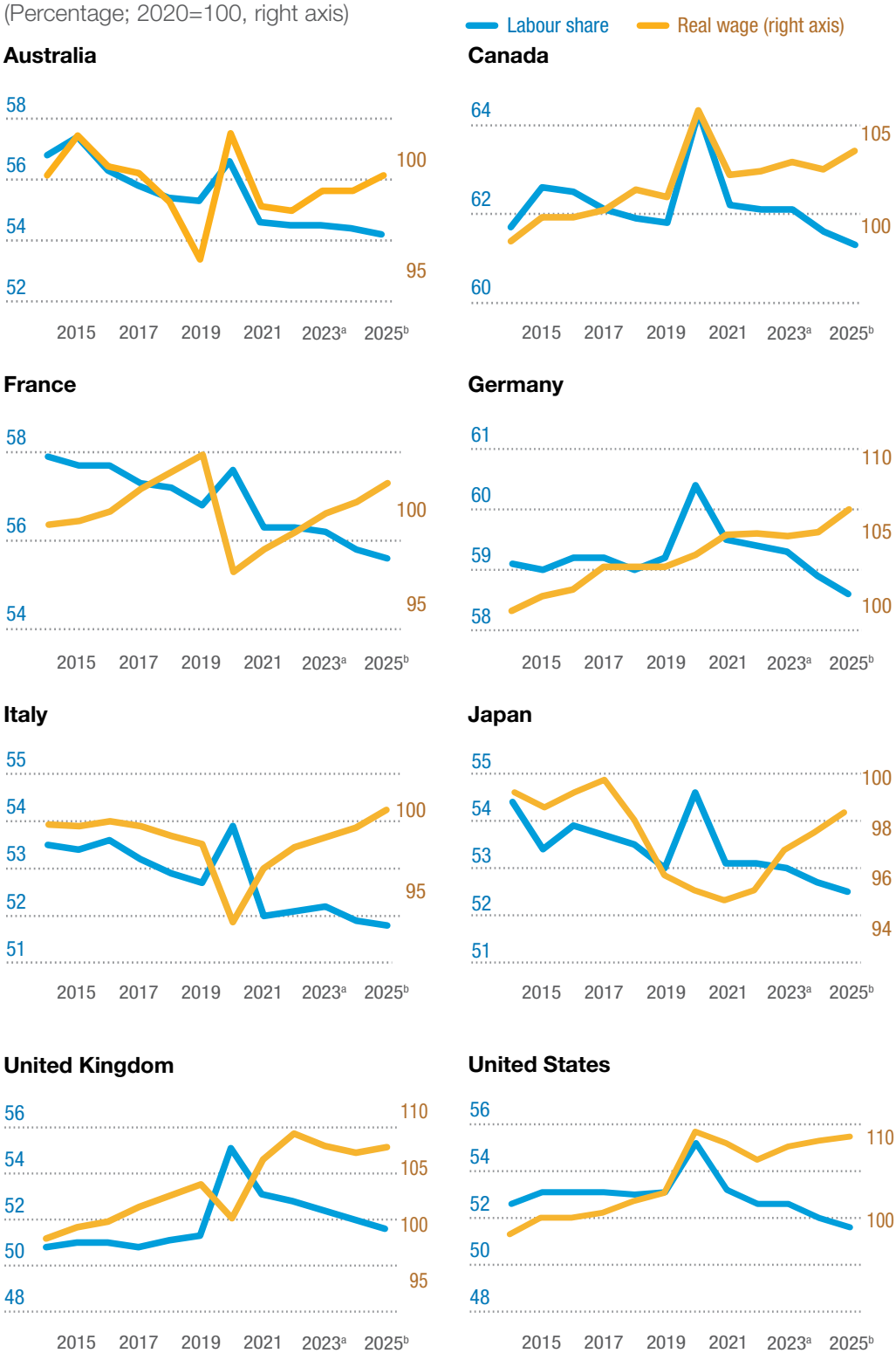
A combined decline in the labour share of income and real wages is particularly troublesome.

All five BRICS economies have seen reductions in the labour share, while real wages in these countries are taking diverging paths (figure I.14). In China and India, rapid economic growth is producing fast productivity growth along the Kaldor-Verdoorn hypothesis (Barbosa-Filho, 2008), which allows for a more dynamic uptick in real wages. The opposite is observed in Brazil and South Africa, where the real wage has stagnated or fallen. The Russian Federation falls between these two poles, with a drop in the labour share and a modest increase in the real wage.

Figure I.13

A universal fall in the labour share unfolds across developed economies amid diverging trajectories in real wages

Labour share of income and real-wage index, selected developed economies
(Percentage; 2020=100, right axis)

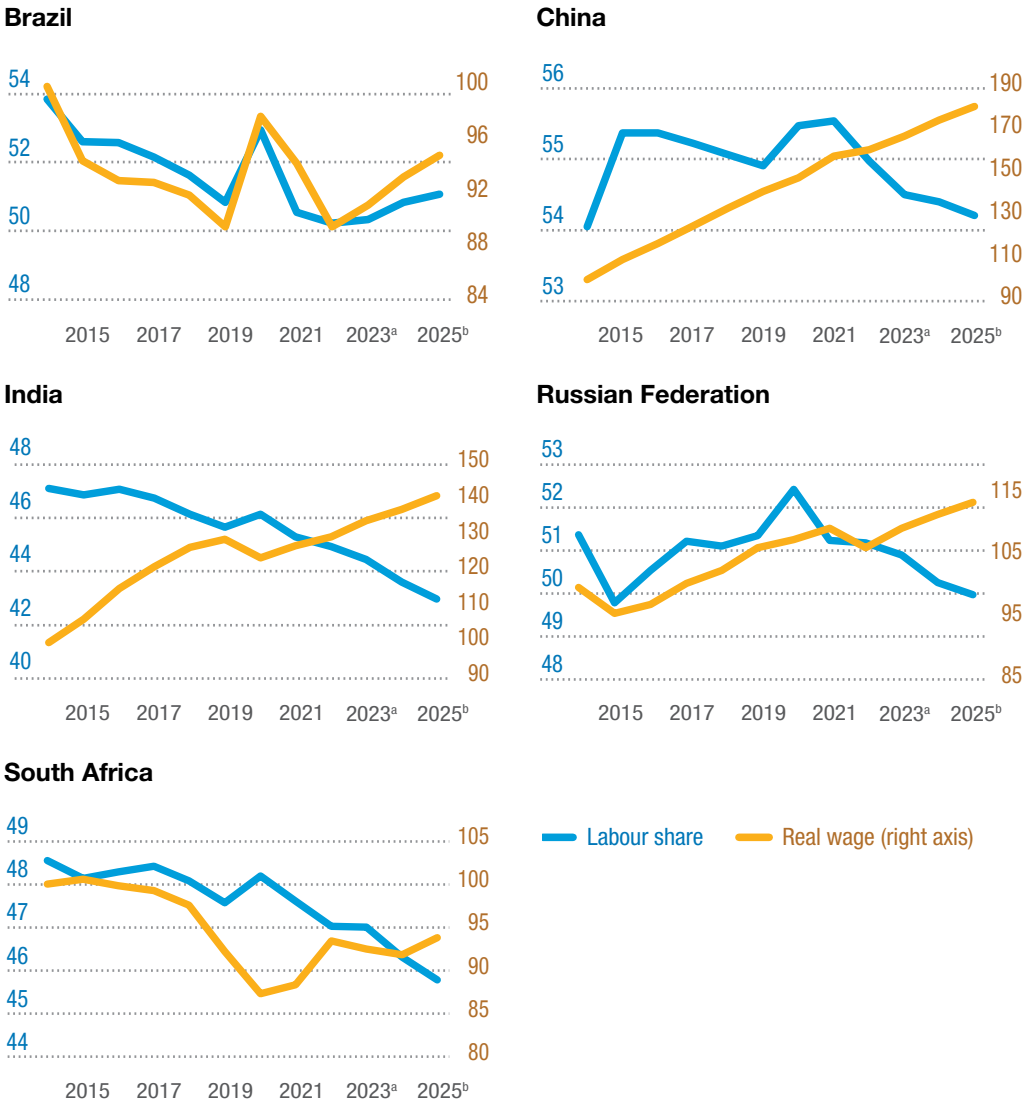


Source: UNCTAD based on the United Nations Global Policy Model.
2023a, 2024a Estimate.
2025b Projection.

Figure I.14

BRICS economies are following trends similar to those in the developed economies

Labour share of income and real-wage index
(Percentage; 2020=100, right axis)



Source: UNCTAD based on the United Nations Global Policy Model.
2023a, 2024a Estimate.
2025b Projection.

Is a reversal in the downward trajectory of the labour share plausible under current circumstances? The prospects are not encouraging. The labour share has trended down across both developed and developing countries since the 1980s, with a corresponding rise in the profit share. If pre-pandemic trends resume, the labour share is likely to continue to decline, with negative consequences not only for a sustainable pick-up in the global economy but also for income inequality (UNCTAD, 2019).

While the functional distribution of income helps to analyse real-wage dynamics, it does not necessarily capture the income share of the bottom and middle part of the income distribution. A substantial proportion of the labour share goes to high-wage workers

The labour share of income is likely to decline, with negative consequences for the global economy and income inequality.

at the top of the income distribution. Conversely, a share of capital income is distributed to the middle through pensions and progressive tax-and-transfer social security systems. Other metrics are required to reveal the distribution of personal income among different strata of income earners.

People at the lower end of the income distribution often bear the brunt of the declining labour share.

Macroeconomic theory and policy are slowly incorporating the dynamics of personal income distribution in their analyses. The main difficulty in doing so lies in the low frequency of, as well as lags in, data on individual distribution. Such data usually come from household surveys and income-tax data that are typically available with a two-to-three-year lag. As a result, data on personal income distribution for 2021 and 2022 are the most recent available, giving a first insight into the impact of the pandemic on personal income inequality.

Based on the World Inequality Database, it is possible to get a glimpse of the changes in personal income distribution in several advanced economies since the pandemic. To facilitate analysis, the total population is divided into four income groups: the low-income group (bottom 50 per cent), the middle class (the next 40 per cent), the upper-middle class (the following 9 per cent) and the rich (the top 1 per cent).

Data on pre-tax personal income distribution in the United States indicate a sharp fall for low-income families, stability for the middle class and a gain for the top 10 per cent, most of which is concentrated in the top 1 per cent (figure I.15). In Italy, the qualitative situation is similar, with an increase for the top 10 per cent and a fall for the bottom 50 per cent. A difference in Italy is that the middle 40 per cent have also lost income share since the pandemic (figure I.15).

The pandemic had a drastically different impact on Germany and the United Kingdom compared to the United States. In the United Kingdom, the bottom 50 per cent and the upper-middle class returned to almost the same income share after the pandemic, while the middle 40 per cent gained and the top 1 per cent lost shares. In Germany, after an initial loss, the bottom 50 per cent and the middle 40 per cent gained income shares at the expense of the top 10 per cent (figure I.16).

The broad fall in the labour share across both developed and developing economies, together with the increasing concentration of income at the higher end of the spectrum in some countries, points to the fact that those at the lower end of the income distribution are often bearing the brunt of the reduction in the labour share. This has fed widespread dissatisfaction and discontent, with disquiet magnified in countries where the real wage has remained below the pre-pandemic trend, as in France, Japan and South Africa.

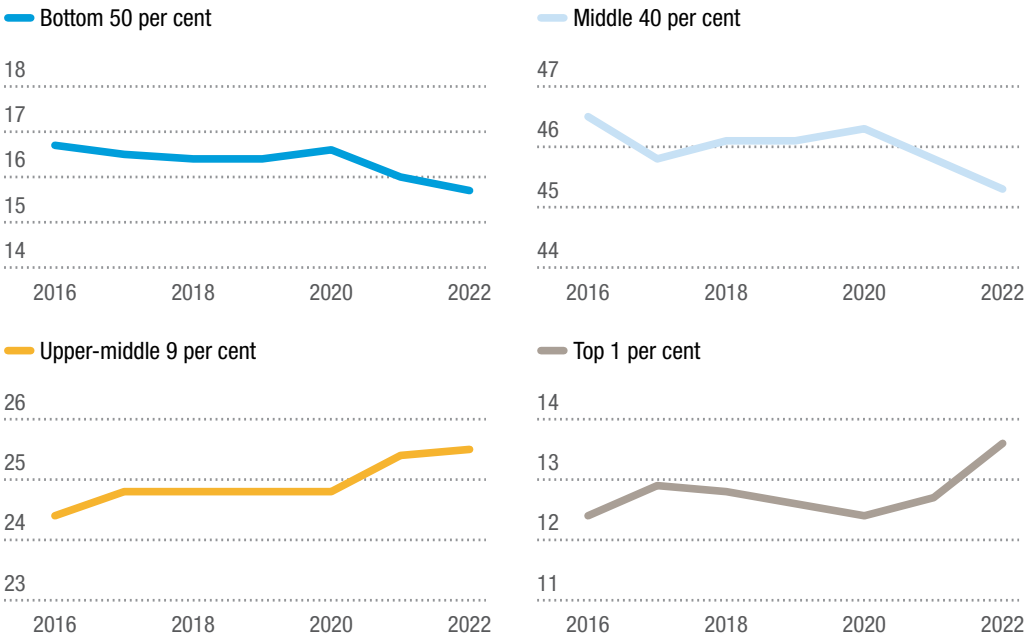
Reversing the trends of a diminishing labour share, growing income inequality and stagnant or declining real wages must be a policy priority in developed and developing countries alike, one addressed through more equitable policy solutions. Concrete commitments to more comprehensive social protection are a necessary starting point. Systematic policy measures to help lower inequalities and deliver more inclusive growth should be essential components of development and growth strategies (UNCTAD, 2023b).

Figure I.15

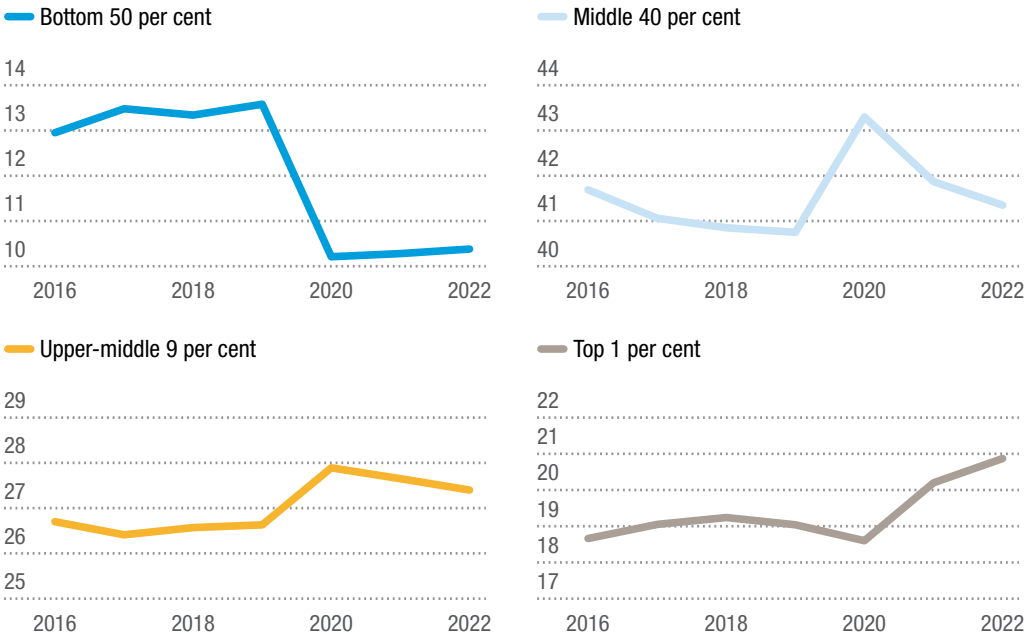
Those with lower income bear the brunt of the decline in the labour share of income in some developed countries

Pre-tax personal income distribution
(Percentage of total personal income)

Italy



United States



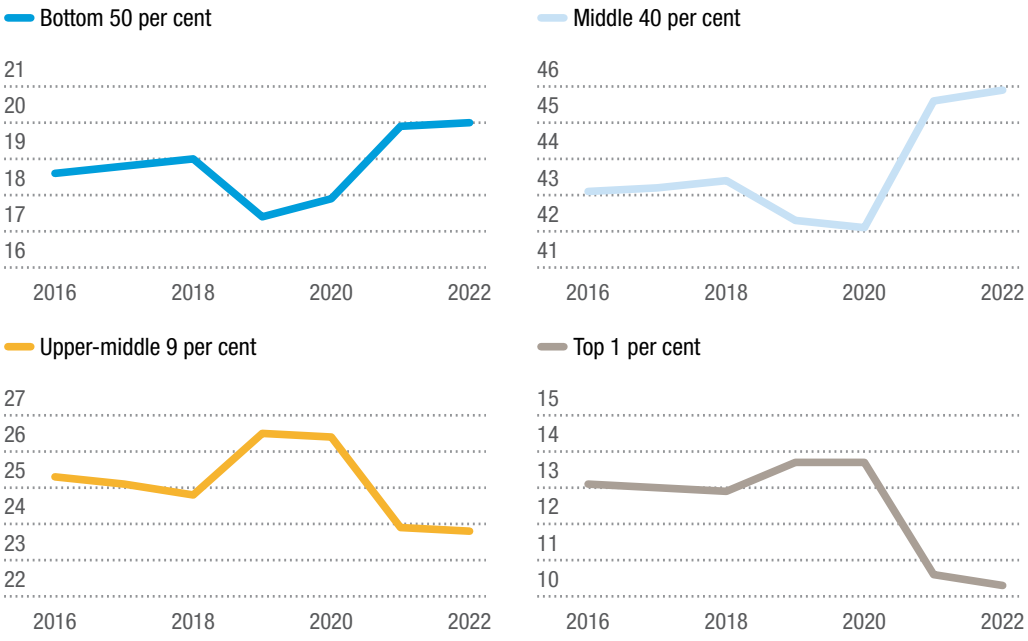
Source: UNCTAD based on the World Inequality Database.

Figure I.16

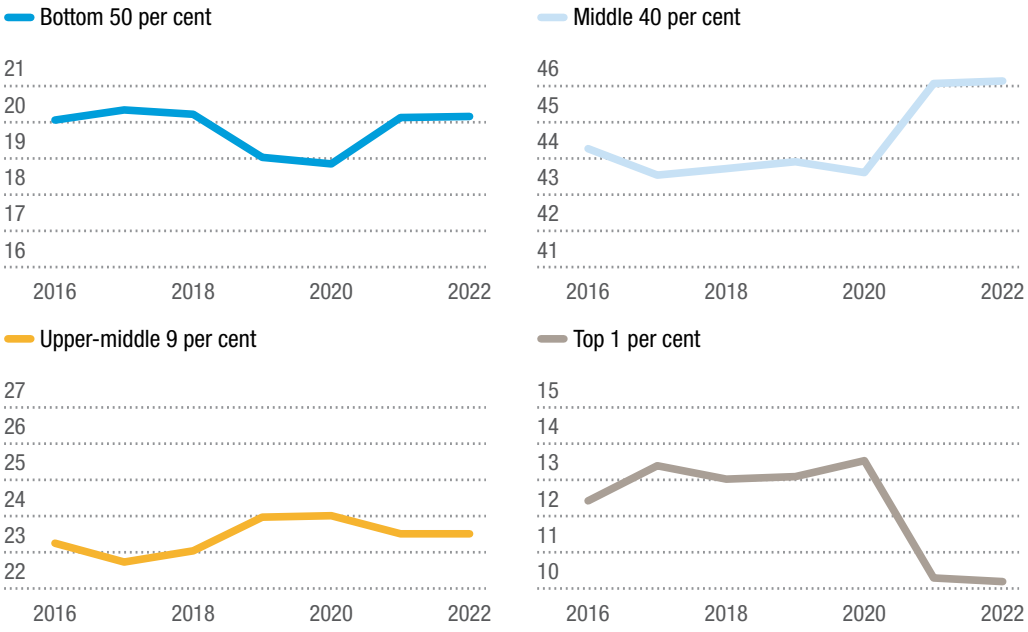
Some advanced economies saw a more progressive evolution in income shares post-pandemic

Pre-tax personal income distribution
(Percentage of total personal income)

Germany



United Kingdom



Source: UNCTAD based on the World Inequality Database.

G. Regional Trends

The Americas

UNCTAD estimates that the economy of the **United States** will maintain its growth rate in 2024 at 2.5 per cent, largely due to three fundamental factors. First, on the fiscal side, investment incentives under the Inflation Reduction Act and the Creating Helpful Incentives to Produce Semiconductors (CHIPS) and Science Act have more than compensated for waning COVID-19 transfers and subsidies (Ahmad et al., 2024). Second, on the monetary side, the Federal Reserve's gradualist disinflation strategy has kept the 10 year real interest rate practically constant through 2023 and 2024, at between 1.5 and 2 per cent, which has allowed a cyclical recovery in residential investment after a double-digit fall in 2023. Third, the artificial intelligence boom has boosted investment in intellectual property, which is expected to register an annual growth of approximately 5 per cent in 2024 and next year.

For 2025, UNCTAD expects the expansion of the United States economy to decelerate to 1.8 per cent, mainly due to a negative fiscal impulse. Although monetary easing could play an important role in changing the macroeconomic outlook, since core inflation indexes are still running at 1.5 percentage points above the Federal Reserve's 2 per cent target, there is still high uncertainty regarding the path and speed of monetary easing after the first rate cut of 50 basis points in September 2024.

Canada is expected to register a slight moderation in its economic expansion, from 1.2 per cent in 2023 to 1.1 per cent in 2024, driven in part by the lagged effects of a relatively more aggressive disinflation monetary policy and fiscal consolidation strategy. In a context of core inflation indexes falling to the Central Bank's 2 per cent inflation target and an almost stagnant economy, the Bank of Canada started cutting its policy rate in mid-2024. A more accommodative monetary stance should help raise GDP growth to 2.1 per cent in 2025.

UNCTAD predicts that in **Mexico**, the growth rate will decelerate from 3.2 per cent in 2023 to 2.0 per cent in 2024 as ongoing restrictive macrofinancial conditions, particularly during the first half of the year, and a weakening external environment tamp down activity. The financial market reaction to uncertain government debt trends has already caused a sharp depreciation of the Mexican peso, which tends to generally have a short-run recessive impact in Latin American economies. For 2025, UNCTAD foresees a further slowdown of the economy of Mexico, to 1.5 per cent. The expected deceleration of the economy in the United States and the likely end of COVID-19-induced nearshoring to Mexico could weigh on economic activity next year. On the upside, the expectation of monetary policy turning expansionary by the end of this year as inflation falls to 4 per cent as well as more expansionary fiscal policy could help to strengthen growth.

In South America, the economy of **Brazil** is expected to decelerate slightly this year, from a growth rate of 2.9 per cent in 2023 to 2.8 per cent in 2024. The slowdown reflects a divergent macroeconomic policy mix, as authorities have pursued a restrictive monetary policy and an expansionary fiscal policy. As a result, inflation seems to have stabilized at 4 per cent, 1 percentage point above the Central Bank target, forcing monetary policy to remain restrictive into 2025. There is heightened uncertainty around the direction of fiscal policy,

particularly after a mini-speculative attack against the currency in the first half of 2024. On the expansionary side, the economy continues to benefit from increasing food and oil exports. These factors may not be sufficient, however, to neutralize decelerating domestic demand. As a result, GDP growth is expected to slow to 2.2 per cent in 2025.

The recession in **Argentina** in 2023, with the economy shrinking by 1.6 per cent, is expected to continue into 2024. GDP is projected to fall by 3.5 per cent this year due to a sharp monetary and fiscal contraction. The recession is part of the Government's disinflation strategy, based on the "expansionary fiscal contraction" hypothesis (Alesina and Ardagna, 1998). Macroeconomic policy included a maxi-devaluation of the domestic currency in late 2023, which has already been eroded by double-digit domestic inflation. The initial change in domestic relative prices benefited the export sector, which has been growing and is expected to pull the economy out of recession in 2025, leading UNCTAD to estimate an expansion of 4.8 per cent for next year. The downside of stabilization has been increased poverty rates and heightened uncertainty around the sustainability of the managed exchange rate. Moreover, external solvency depends on IMF support. The potential for another maxi-devaluation of the Argentine peso could inhibit growth prospects in 2025.

Largely due to restrictive monetary and fiscal policies, the largest Andean economies experienced a sharp deceleration in 2023, with almost zero growth in **Colombia** and **Peru** and a mild recession in **Chile**. A fall in inflation in these countries will be accompanied by a recovery in growth in 2024. Furthermore, monetary easing from mid-2024 onwards, together with competitive exchange rates and favourable terms of trade, could help maintain GDP growth in 2025. On the downside, high exposure to external shocks, particularly from sudden changes in the interest rate in the United States, could push the Andean economies back to slow growth in 2025.

European Union

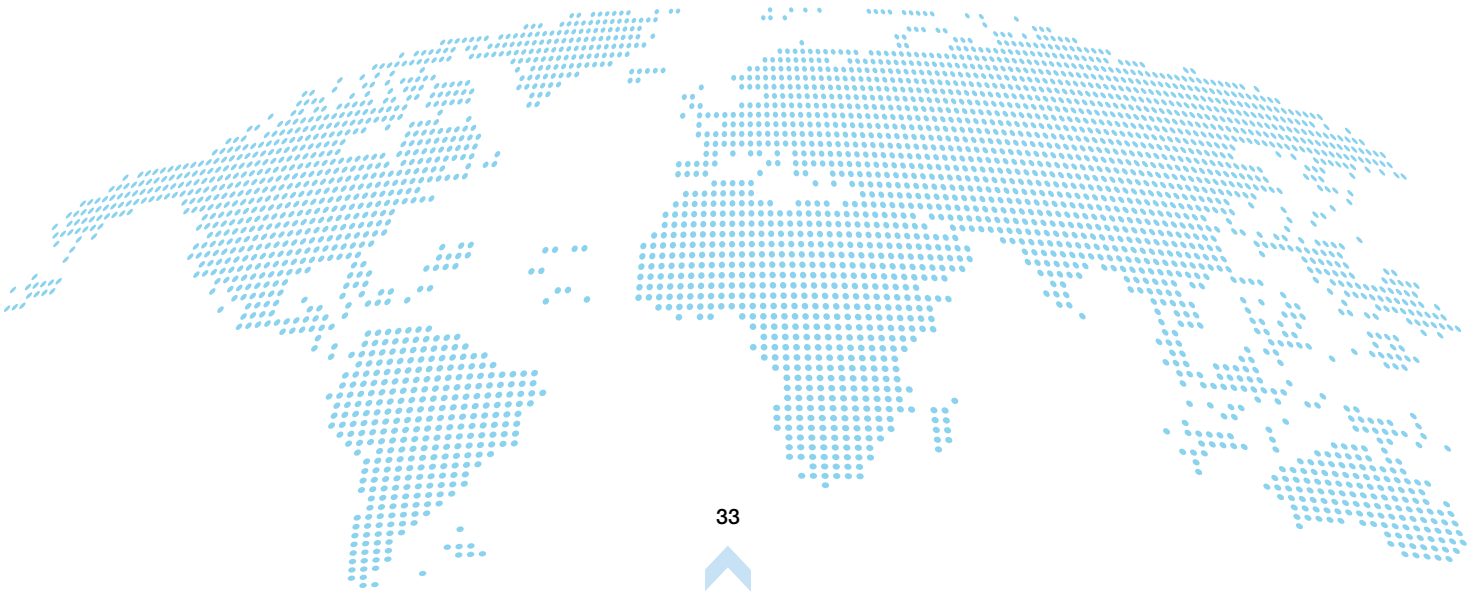
UNCTAD expects GDP growth in the economies of the European Union to pick up in 2024 relative to the 0.5 per cent expansion in 2023. But rates are expected to remain relatively weak at 1 per cent. Improved performance is mostly driven by stronger activity in the services sector. The European Central Bank decision in June to finally begin monetary easing by cutting its key policy rate by 25 basis points should help to partially ease financing conditions. The move puts the euro area ahead of the United States in the monetary easing cycle, as the latter delayed the start of its own process. Since cumulative rate increases by the European Central Bank totalled 450 basis points over the past two years, however, the policy rate remains historically high. This is reflected in ongoing high borrowing costs for businesses and households across the euro area. Additionally, the withdrawal of fiscal support measures introduced to mitigate increased energy prices are reflected in a tightening fiscal policy stance in 2024.

UNCTAD foresees growth picking up further in 2025, to 1.6 per cent as domestic demand strengthens amid gradual monetary policy easing and subsequent lower financing costs. Ongoing tight fiscal stances, however, would continue to hinder growth. The European Union decision in July 2024 to impose tariffs of up to 38 per cent on imports of Chinese built electric vehicles risks setting off tit-for-tat measures that could include retaliatory tariffs on exports from the European Union to China. Such a development could have a strongly adverse impact on the external sectors of a number of European countries for which China is a major export destination.

UNCTAD estimates that economic expansion in **France** will decelerate marginally from 1.1 per cent in 2023 to 1.0 per cent in 2024. Ongoing high interest rates continue to weigh on private investment and consumption while subdued external demand from major trading partners dampens economic activity. Two rounds of spending cuts announced in the first half of the year, totalling 20 billion euros (approximately 1 per cent of GDP), will be reflected in slowing public consumption and investment spending. The Olympic Games in Paris provided a moderate boost to GDP growth in the third quarter. UNCTAD expects the French economy to rebound slightly in 2025, to register growth of 1.3 per cent, as falling inflation and further monetary easing help to stimulate private spending.

In **Germany**, UNCTAD predicts a minor improvement in the growth rate to 0.2 per cent in 2024, after the 0.2 per cent contraction in 2023. The drag on the economy from elevated interest rates has been recently compounded by heightened policy uncertainty regarding the financing of planned investment incentives for the green transition, which could in turn hamper investment spending. The uncertainty is due to a Federal Constitutional Court ruling at the end of 2023 that determined the use of special funds to finance investments as unconstitutional, thus reducing available resources from the Climate and Transformation Fund by 60 billion euros. The knock-on effect may be to greatly reduce public investment spending and hinder fiscal incentives for private investments in the green transition. This is of particular concern given the investment deficit Germany currently exhibits compared to other similar developed economies. This deficit is likely to widen as investment spending on the green transition as well as needed transport infrastructure and the digital transition may continue to lag behind levels of the country's peers. UNCTAD estimates that growth will see a moderate uptick up in 2025, to 1.2 per cent, largely due to easing monetary conditions and stronger household spending.

UNCTAD expects **Italy** to maintain its pace of growth from last year and to register an expansion of 0.9 per cent in 2024. The combination of high inflation and low wage growth has resulted in stagnating real wages, which continue to weigh on private consumption and investment spending. This has been further compounded by continuing tight financial conditions and the withdrawal of exceptional fiscal measures introduced in the wake of the energy crisis. Recent strength in real-estate investment is likely to soften as generous subsidies to the construction sector, known as the "superbonus", are phased out. Partially offsetting these negative trends is increased public investment from the European Union's Next Generation funds. UNCTAD foresees a broadly similar expansion of the economy in Italy in 2025, at 1 per cent, as the easing of financing conditions and improved external demand from some principal trading partners could offset the prospect of a further tightening in fiscal policy.



United Kingdom

Although improving from the almost flat growth performance of 0.1 per cent registered in 2023, the United Kingdom, based on UNCTAD estimates, will continue to exhibit a weak expansion in 2024, at 0.9 per cent. The lack of dynamism is largely due to continuing softness in private consumption, in the context of the ongoing albeit improving cost-of-living crisis as well as trade frictions from the Brexit process that continue to hamper exports. The monetary stance of the Bank of England has remained restrictive; the start of the expected easing cycle was delayed repeatedly despite inflation returning to the 2 per cent target in May. The bank rate was finally cut by 25 basis points in August. As a result, both business and consumer spending continue to be held back by high borrowing costs. Government spending remains flat with persistent shortfalls in public expenditure on services and investment outlays.

UNCTAD expects growth to pick up to 1.4 per cent in 2025 as lower inflation and reduced interest rates will help to boost household spending. The prospect of new public investment spending on green energy and infrastructure by the incoming government could also spur growth. Ongoing trade frictions, however, could continue to have a dampening impact on exports.

Russian Federation

UNCTAD estimates that the Russian Federation will register growth of 3.5 per cent in 2024 compared to 3.6 per cent in 2023. Economic activity is being mainly driven by growing personal incomes and consumer spending. The latter results from a delayed reaction to suppressed demand during 2022 and 2023 and a significant fiscal stimulus last year as well as tightening labour markets. The estimated workforce deficit was approximately 1.7 million workers in mid-2024; the unemployment rate reached a record low of 2.6 per cent. Investment demand is being sustained by previous fiscal stimuli and high corporate profits, although both are likely to plateau through the second half of 2024. Tight credit and foreign exchange policies have kept inflation rates between 4.3 and 4.8 per cent in 2024. The rouble, while stable during the year, is nevertheless weathering the adverse impacts of capital flight as well as heightened demand for foreign currency for purchases of foreign-owned assets in the country and increased budgetary expenditure.

UNCTAD foresees a deceleration of growth in 2025, to 1.5 per cent, as a tightening credit environment internally, expected increases in business taxes and growing trade and financial pressures weigh on economic activity.

East Asia

UNCTAD estimates a moderation in the growth rate in East Asia to 3.9 per cent this year, compared to 4.2 per cent in 2023. The slowdown at the aggregate regional level is largely driven by the evolution of the economy of **China**. For 2025, UNCTAD expects the region's growth to slow further, to 3.7 per cent.

UNCTAD envisages a modest deceleration in economic activity in China, from 5.2 per cent in 2023 to 4.9 per cent in 2024. Growth has been bolstered by strong

net exports and the resilient performance of the industrial sector. Strengthening investment in manufacturing, particularly in high-technology industries, has buoyed growth. Both employment and corporate profits have registered slight improvements. Ongoing sluggishness in the real estate sector as well as subdued consumption are tempering economic expansion, however. Consumption has yet to recover to its pre-pandemic trend, indicating continuing fragility in terms of consumer confidence and expectations. The real estate sector, once a pillar of growth, has contracted sharply since early 2022. The trend continued into 2024, with both real estate investment and sales shrinking significantly during the first half of the year, by 10 and 25 per cent, respectively.

The yet-to-be-stabilized housing market constitutes a significant risk and has become a policy focus of authorities. Local government debt, which is closely linked to the housing market, represents a further downside risk. In response to these issues, the Government is scaling up rescue policy measures to stabilize the real estate market. Similarly, on the monetary side, the Central Bank has enacted further measures to shore up the real estate market and boost consumption. The measures include cuts to reserve ratio requirements, the prime rate, the seven-day reverse repurchase interest rate and the one-year medium-term lending facility. The monetary authority has earmarked two relending loan facilities and provided 300 billion renminbi for affordable housing as well as 500 billion renminbi for innovation and technology upgrading.

UNCTAD expects a further moderation in growth in 2025, to 4.6 per cent. Increasing trade tensions, particularly with the United States and European Union around electronic vehicles and related products, is causing growing uncertainty for the external sector. The diversified nature of trade partnerships and products, strong capacities across a wide array of green energy products, and technical and supply chain advantages should help to expand exports. The third Plenum of the Communist Party of China Central Committee, held in July, adopted its Resolution on Further Deepening Reform Comprehensively to Advance Chinese Modernization. It includes structural reform proposals to promote "high-quality economic development". Should China stabilize the real estate sector towards the end of the year and effectively advance its reform proposals, it is still possible for the economy to maintain reasonable growth in the medium term.

UNCTAD estimates that the **Republic of Korea** will see an uptick in its growth rate to 2.3 per cent in 2024, compared to 1.4 per cent in 2023. The acceleration largely reflects the strong performance of exports, including a pick-up in inward tourism flows. Despite significant easing in inflation compared to last year, however, the Central Bank has maintained its tight monetary stance, and high borrowing costs continue to depress domestic demand. High levels of household debt are hampering household spending and remain a concern for policymakers. The restrictive monetary stance accompanies a similarly tight fiscal policy; government expenditure is expected to record its lowest annual increase in the last 20 years. For 2025, UNCTAD foresees a moderation in the growth rate to 2.1 per cent, with an expected slowdown in exports and ongoing sluggish domestic demand expected to weigh on economic activity.

UNCTAD estimates that **Japan** will register a significant slowdown in its growth rate from 1.8 per cent in 2023 to 0.9 per cent in 2024. The strong external demand for goods manufactured in Japan that emerged during the post-COVID-19 phase has not been sustained. Resulting sluggishness in the external sector along with the country's ageing population is moderating economic growth. Although wages are rising at the highest rate in more than 30 years, the impact on consumer spending is expected to be muted largely due to the heavier social burden and increase in the number of pensioners. Rises in consumption to date have been

mostly driven by households drawing down savings accumulated during the pandemic.

In a significant change in policy stance, the Central Bank of Japan hiked interest rates in March 2024 for the first time in 17 years. The increase put an end to an eight-year period of negative interest rates and marked the start of efforts towards policy normalization. The decision to increase the policy rate again in July, to 0.25 per cent, surprised markets and propelled the yen higher. Shrinking interest rate spreads with other major economies sparked a rapid sell-off as heavily leveraged traders and investors exited carry-trade and related markets. The prospect of further rate hikes was mitigated by assurances from the Central Bank Governor that policy rates would not rise again while markets remained unstable. On the fiscal side, in late 2023, the Government announced a $113 billion package of tax cuts and subsidies for fuel and utility bills along with major commitments to achieving net-zero carbon emissions.

UNCTAD expects the economy in Japan to maintain its growth rate in 2025 at 1 per cent, as the normalization of monetary policy could constrain domestic demand and inhibit growth.

South Asia

South Asia's economic perspectives remain strong, supported by robust growth in India and recoveries in Pakistan and Sri Lanka. The regional economy will expand by 5.7 per cent in 2024, compared to 6.1 per cent in 2023. UNCTAD expects the region to grow at a slightly slower but elevated pace of 5.5 per cent in 2025, in sync with the evolution of its largest economy, India, and supported by economic rebounds in countries recovering from extreme climate events or prolonged political instability and debt distress, namely, Pakistan and Sri Lanka. External imbalances and growing dependence on extraregional fossil fuel energy imports will keep the region vulnerable to inflationary pressures, however, and political coalitions could complicate sustained public spending.

Economic growth in **India** will remain elevated at 6.8 per cent in 2024 compared to 7.7 per cent in 2023. This expansion is supported by continued strong public and private investment and consumption as well as rising exports of services. Despite the latter, along with increased exports of certain goods, such as chemicals and pharmaceuticals, the structural current account deficit in India will persist, owing to relatively weaker external demand and high fossil energy import bills. As the world's most populous country and third-largest energy consumer, India is simultaneously expanding its domestic non-fossil and fossil fuel energy supply to support growing economic output. While the former has increased fourfold over the last eight years, the latter also grew rapidly; domestic coal production rose by 80 per cent, reaching a new record of 1 billion tons in 2024. This rise was driven by public investment in the wake of the war in Ukraine and the resulting energy crisis. As inflation is expected to decline to 4 per cent by the end of the year, the Reserve Bank of India may initiate monetary easing and trim its repurchase rate. The rate has remained unchanged at 6.5 per cent since early 2023, maintaining high financing costs for leveraged corporates. As public spending may exceed revenues by 5.1 per cent in the current fiscal year, and absent financial instability or external shocks, GDP growth is projected to remain strong at 6.3 per cent in 2025.

South-East Asia

UNCTAD estimates an acceleration in the growth rate in South-East Asia from 3.9 per cent in 2023 to 4.5 per cent in 2024 as a gradual recovery in global demand for electronics helps to boost the region's trade. Ongoing tight monetary stances amid fears of capital outflows and depreciation pressures on local currencies given restrictive monetary conditions elsewhere, particularly in the United States, continue to hold back domestic demand within the region. UNCTAD expects growth to remain fairly stable in 2025, at 4.4 per cent, as domestic demand firms up in a context of declining borrowing costs and supports growth.

UNCTAD estimates that **Indonesia** will continue to grow at a brisk pace in 2024, at 5.1 per cent compared to 5.0 per cent in 2023. Private consumption continues to be the main driver of growth despite elevated interest rates. The Central Bank further increased its policy rate in April to avoid significant interest rate differentials with the United States in light of its ongoing tight monetary stance. Such differentials could put further downward pressure on the Indonesian rupiah, which has historically been particularly sensitive to divergent interest rate paths. The high cost of borrowing resulting from a restrictive domestic monetary stance is reflected in slowing private investment expenditures.

Increased fiscal spending on infrastructure plans and social assistance schemes is helping to support growth. Rising tourism arrivals, particularly from within Asia, is bolstering services exports, while increasing volumes of base metals exports, particularly nickel, enhance the external sector balance. UNCTAD expects the Indonesian economy to maintain strong growth in 2025, with the prospect of lower interest rates as well as an improving external context helping to shore up growth at 5.2 per cent.

UNCTAD expects an acceleration in the growth rate of **Malaysia** from 3.6 per cent in 2023 to 4.4 per cent in 2024, as falling inflation and a national cash transfer programme help to boost private consumption. Investment expenditures remain robust as progress continues on a series of multi-year infrastructure projects. The services sector is benefiting from the continuing recovery of tourism inflows, which are now nearing pre-pandemic levels. Ongoing tight international monetary conditions, however, continue to put depreciation pressure on the Malaysian ringgit. UNCTAD estimates that economic activity will expand at a rate of 4.0 per cent in 2025, with private consumption and investment expenditures continuing to provide the basis for growth.

In **Thailand**, UNCTAD estimates a significant uptick in growth to 2.9 per cent in 2024 compared to 1.9 per cent in 2023. Robust private consumption is being helped by a strong labour market, while services exports are seeing dynamic growth as the tourism sector continues to rebound strongly. Public spending is set to pick up with the approval of the fiscal budget after significant delays. A planned digital cash transfer programme could provide additional impetus to household consumption. Investment spending broadly remains muted, although certain sectors, namely electronics and electric vehicles, continue to attract significant investments. UNCTAD expects the expansion of the economy of Thailand to remain steady at 2.9 per cent in 2025.

Viet Nam continues to register among the fastest growth rates in the region, with economic growth accelerating from 5.0 per cent in 2023 to 5.6 per cent in 2024. A series of wage reform measures is helping to improve household incomes and boost private consumption expenditures. The ramped-up disbursement of public investment funds supports investment outlays. While the country is less reliant on tourism inflows than other countries in the region, the ongoing upturn in international arrivals provides a boost to

the external sector. Growth in the property sector remains subdued due to tight credit conditions and continues to act as a drag on growth. UNCTAD expects the economy of Viet Nam to expand by 5.4 per cent in 2025, with the prospect of a more accommodative monetary stance helping to ease the current credit crunch and spur recovery in the construction sector.

Western Asia

UNCTAD estimates that Western Asia will register growth of 2.4 per cent in 2024, up from 2.0 per cent in 2023. The pick-up in economic activity results mainly from the stabilization of oil prices and a rebound in major oil-exporting economies. Significant risks remain as widening conflicts spur tensions throughout the region, with ripple effects for international shipping in the Red Sea.[4] While a significant risk of escalating tensions could impact economic performance across the entire region and beyond, the effects are particularly detrimental to certain countries, namely Israel, Lebanon, Yemen and the State of Palestine.[5] In the absence of a further escalation of tensions, the region's growth is projected to accelerate to 3.9 per cent in 2025.

UNCTAD expects economic growth in **Saudi Arabia** to rebound to 1.7 per cent in 2024, after a historic 0.8 per cent contraction in 2023. As the Organization of the Petroleum Exporting Countries (OPEC) manages oil output, including through production limits to maintain oil prices between 70 and 90 United States dollars per barrel, oil export revenues will likely move in tandem with external demand. Non-oil sectors are forecast to contribute to growth even though investment in pharaonic projects in the Neom development is being curtailed, dimming expected activity in construction and related upstream and downstream sectors. Investment in renewable energy still represents less than 20 per cent of total energy investment, delaying much needed diversification and the transition away from fossil fuels. In 2025, Saudi Arabia is expected to grow by 4.7 per cent as strong activity in both the oil and non-oil sectors – particularly tourism, logistics and manufacturing – will serve to boost growth.

UNCTAD estimates that **Türkiye** will register growth of 3.5 per cent in 2024 compared to 4.5 per cent in 2023. Domestic demand has suffered from the effects of spiralling year-on-year inflation, which peaked at 75 per cent in May. The Central Bank began monetary tightening in June 2023 and hiked the policy rate from 8.5 to 50 per cent by March 2024, where it has remained. High financing costs continue to adversely impact demand and employment. Despite the tight monetary stance, the Turkish lira has continued to depreciate against other hard currencies, such as the United States dollar. While this devaluation has increased the servicing costs of foreign currency-denominated external debts – with elevated levels held by private companies – the lower value of the currency has boosted exports and weakened imports, except for fossil fuel energy imports. Turkish exporters of manufactured goods and machinery and transport equipment have performed particularly well, along with the tourism sector.

Current monetary tightening in Türkiye is expected to end in the second half of 2024, resulting in a gradual recovery of consumption and strengthening of economic activity in the coming year. In this context, UNCTAD expects the economy to grow by 3.8 per cent in 2025.

[4] For further information, see UNCTAD (2024a).

[5] For further information on the impact of the Israeli military operation on Gaza and the West Bank, see UNCTAD (2023a, 2024b).

Africa

Africa's growth is set to remain subdued after decelerating gradually during 2021–2023. As recent efforts to restore macroeconomic stability should start to yield some positive results from the second half of 2024 onwards, especially in several large economies, aggregated economic activity for the continent is expected to expand from a more sluggish 3.0 per cent in 2024 to 3.2 per cent in 2025. These rates, however, do not exceed by much the 2.4 per cent annual growth of Africa's population in recent years. GDP growth will therefore remain short of what is needed to make major strides towards economic development and structural transformation. Various difficulties weigh on economic prospects and livelihoods across the continent.

Often confronting an unfavourable economic environment on all three levels – global, regional and national – following the COVID-19 pandemic, African policymakers have frequently had to swiftly undertake policy actions to manage complex challenges. While there is scope for well-calibrated structural reforms to lift growth over the medium term, hasty shifts in policy stances have often led to significant economic disturbances in the short run, disproportionately affecting ordinary African citizens, particularly the poor.

One concern relates to deteriorating external accounts in many African economies. This has triggered sharp falls in the value of several African currencies with managed floating or fixed exchanges rates amid weaker import cover ratios and subdued financial flows. These significant depreciations, often coupled with limited supplies of basic staples and sometimes also the uncontrolled provision of liquidity, have pushed inflation rates far above their historical averages, as is the case in Angola, Egypt, Ethiopia and Nigeria, for instance. In reaction, several monetary authorities raised interest rates to levels between 20 and 30 per cent in August 2024.

On the fiscal front, the current stance across the continent is typically geared towards consolidation in response to challenging debt situations and higher financing costs, declining aid flows, large budget deficits compounded by limited success in scaling up domestic resource mobilization after COVID-19, and subdued export revenues, including for some large hydrocarbon-exporting economies that have registered declining export volumes.

Violent protests have emerged across the continent in response to economic hardship, elevated inflation rates, particularly for basic staples, and hasty reforms. In Kenya, for instance, deadly demonstrations pushed the Government to withdraw a controversial tax bill. Overall, this highlights the complexity of implementing reforms when economies are experiencing tough conditions.

More broadly, even as inflationary pressures begin to gradually abate across the continent, other key factors continue to hinder development. These include ongoing conflicts, including in Libya as well as several areas of Sahelian countries and the Middle Africa region. The negative impacts of climate change and extreme weather shocks are expected to increase levels of acute food insecurity in 2024 and 2025, even as 33 African countries already need external food assistance and the region's total annual cereal production is expected to drop by 3 per cent in 2024 compared to 2023. El Niño-linked droughts have caused widespread crop damage and wilting, especially in Southern Africa (FAO, 2024).

In **South Africa**, UNCTAD estimates that a more reliable electricity supply and improving logistics is likely to support a meagre rebound of the economy, from 0.6 per cent growth in 2023 to 0.9 per cent in 2024. As in Egypt and Nigeria – the two other major African economies that have recorded lower growth rates in recent years compared to historical averages – significant headwinds remain for the South African economy. UNCTAD expects relatively weak growth to persist in 2025, at 1.4 per cent.

Oceania

In **Australia**, UNCTAD estimates that the economy will continue its gradual deceleration and register 1.4 per cent growth in 2024, compared to 2.0 per cent in 2023. Most of the slowdown can be explained by the tight monetary policy enacted to bring post-pandemic inflation back to target, which could take some time as unit labour costs grew at 6 per cent year on year as of mid-2024. Consumer inflation is expected to close this year at around 3 per cent, 1 percentage point higher than the Central Bank's 2 per cent target. The expectation of monetary easing next year will help GDP growth to rebound to 2.1 per cent in 2025.

Due to a tight monetary policy and a negative fiscal impulse for this year, **New Zealand** will grow by only 0.9 per cent in 2024, according to UNCTAD estimates, slightly higher than the 0.6 per cent registered in 2023. As in Australia, inflation is expected to fall gradually through 2024 and 2025, resulting in an expected loosening of monetary policy next year. UNCTAD expects growth to pick up to 2.0 per cent in 2025.

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2024 Trade and development report

Chapter II

The illusion of a rebound: International markets in 2024

Growth in merchandise trade is expected to rebound about 2 per cent in 2024 after declining by 1.2 per cent in real terms in 2023. The dynamic trends observed during the first quarter of 2024 will slow through the end of the year as economic deceleration is anticipated in the world's two largest economies. Further, the front-loading of orders in part drove early 2024 momentum.

Several countries, both developed and developing, have introduced trade restrictive measures related to China in 2024.

Trade in services remains more dynamic than trade in goods. Transport and travel components grew at double-digit rates during the first quarter of 2024, with the rest of commercial services growing about 5 per cent.

International prices of many commodities have receded from their 2022 peaks, yet they remain high by historical standards.

In early 2024, net capital flows to developing countries recovered, partly because of a rebound of sovereign bond issuances in developing regions albeit limited in Africa. Borrowing costs, however, are above historical averages.

United Nations

Key policy takeaways

- **Developing country policymakers need to look beyond manufacturing-led exports in an era of subdued merchandise trade and rapid digital progresses** to enable the creation of quality jobs in the services sectors, including in non-tradable services.
- **A rapid phase out of fossil fuels is an essential condition for implementing climate objectives of the Paris agreement and sustainable economic diversification.** Continuing subsidies for fossil fuels and the profitability of fossil fuels extraction and trade imperil the green transition.
- **UNCTAD is offering a set of transformational proposals** along the five stages of the debt life cycle to reduce the costs of development financing and diminish sovereign debt vulnerabilities in developing countries.

A. Introduction

In 2024, major international markets rebounded, including in the trade of manufactured products, services, primary commodities and financial assets. After several turbulent years, commodity prices have partly receded from their 2022 highs. Net capital flows to developing countries turned positive during the first quarter of 2024, and growth in merchandise trade returned to positive territory.

Beneath the surface, however, lie major challenges for policymakers, particularly in developing countries. Geopolitical tensions, global warming, and financial and currency instability compound discontent with a global economy weakened by crises and underinvestment (chapter I).

Uncertainties weigh on international markets and risk distracting policymakers from addressing long-term challenges.

As a result, the current period is marked by high uncertainties. Immediate problems divert attention from long-standing challenges. In many areas, this undermines multilateralism and global economic stability. Changes in monetary policies by the central banks in advanced economies, coupled with the rapid unwinding of financial positions, jeopardize international trading, monetary and financial systems, as market turbulence in August 2024 showed. Most crucially, uncertainty, geopolitical tensions and weakened macroeconomic foundations do not provide a favourable economic and financial environment for development.

This chapter reviews current trends and specific challenges in international trade (section B), primary commodities (section C) and capital flows (section D). It also identifies major issues that together constitute a core challenge for development policy and require further multilateral attention:

- Reorientation of development strategies to go beyond manufacturing-led exports for developing countries and allow broad-based creation of quality jobs in an era of subdued merchandise trade and rapid digitalization.
- The high profitability of fossil fuel extraction and trade that drives current “brown” energy investment and exports as well as continued subsidies for fossil fuels imperil the much needed push for a green transition.
- Changes to the global financial architecture along the five stages of the debt life cycle are needed to reduce the costs of development financing.

B. International trade: The 2024 revival is not the end of the tunnel

1. Geopolitical tensions and policy uncertainty are likely to limit the rebound

After stagnating in 2023, international trade in goods and services is expected to rebound by 2 to 3 per cent in real terms in 2024.[6] Merchandise trade, which contracted 1.2 per cent in real terms in 2023, was the main cause for the poor performance of the broad aggregate in 2023. This is because gross flows of goods still account for more than 75 per cent of global trade in aggregate. The drop reflected a mixture of trade tensions, subdued global demand, changes in inventories and high base effects relating to the temporary shift in expenditure towards durable goods during the COVID-19 pandemic (UNCTAD, 2024h). As a result, the elasticity of global merchandise trade vis-à-vis economic output plunged into negative territory.

That change was unprecedented in recent history. Apart from 2023, global trade had contracted only twice on an annual basis in more than four decades, in 2009 and 2020. On both occasions, however, world gross product also shrank in parallel. Hence the elasticity – which refers to the ratio of the percentage change in trade volume to the percentage change in world gross product – remained positive. What made 2023 extraordinary was the fact that merchandise trade contracted while global economic activity was still growing.

Beyond these arithmetic considerations, this development highlights the structural slowdown that merchandise trade has experienced since the global financial crisis. By contrast, trade in services has been more dynamic.

In 2023, global trade in services grew by about 5 per cent in real terms, highlighting the mounting importance of international trade in services. These elements explain why global trade supporters have recently put more emphasis on international services. As the share of services in global trade reached almost 25 per cent in 2023 and is projected to grow further,[7] expectations are high in some policy and academic communities for international services to become the new growth engine.

There is no consensus, however, that trade in services can be the new principal developmental lever in developing countries. Rather, there is a growing recognition, shared by leading academics, that strengthening productivity and the creation of quality jobs in labour-absorbing sectors such as care, retail, education and other personal services, which tend not to be internationally traded, should be the cornerstones of future development strategies. This seems to be the only remaining way to ensure that a large part of the currently underemployed labour force can register increased real wages over time. This section delves more deeply into these issues.

[6] Providing a precise estimate for 2023 will only be feasible after all national accounts data for that year have been released. Preliminary estimates of key price indices and already released trade figures for subcomponents of trade in goods and services in nominal terms point, however, to a subdued expansion or even a mild contraction in real terms of this broad aggregate in 2023.

[7] The value of trade in services stood slightly below 25 per cent in 2023, even though the World Bank and WTO (2023) find that services activities – albeit not only deriving from trade in services – currently account for roughly half of global trade in value added terms. These two approaches do not contradict themselves, however, because a significant part of the value added emanating from services is necessary to produce manufactured goods that are internationally traded and, thus, are counted under goods instead of services in tracking gross trade flows.

Trade in goods at a time of geopolitical turmoil

Growth prospects for world merchandise trade for 2024 have returned to positive numbers. The UNCTAD nowcast model predicts that export revenues will reach almost $32 trillion in 2024. Yet regional developments have been uneven. Although revenues from world trade are growing again, they are unlikely to surpass their record level of 2022 (UNCTAD, 2024c). This is primarily because, in real terms, exports in most developed countries have either stagnated or even declined recently (figure II.1), but also because key international commodity prices have also receded (section C).

In Europe, a key player in international trade, the euro revenues of goods exports from the euro area were still 3 per cent lower during the first quarter of 2024 compared to the same period the previous year. This occurred even though inflation mechanically boosted revenues. More precisely, each of the 12 largest exporters of this group registered a decline between these two periods (ECB, 2024). In the United Kingdom, export revenues, in sterling, were also down by 4 per cent (United Kingdom, 2024). Overall, this highlights subdued demand from key partners, such as China, as well as the difficulties of European exporting firms in maintaining their shares of world markets.

The robust trends in merchandise trade in early 2024 will likely dwindle.

The robust trajectory observed in East and South-East Asian developing economies, by contrast, has contributed most to the expansion of merchandise exports during the first half of 2024. Specifically, merchandise export revenues in dollar terms of the world's largest merchandise-exporting economy have exhibited robust expansion, with exports from China growing about 7 to 9 per cent on a year-on-year basis by mid-2024 owing to increased shipments of cars and semiconductors.

The adoption of increased protectionist actions was not restricted to OECD economies.

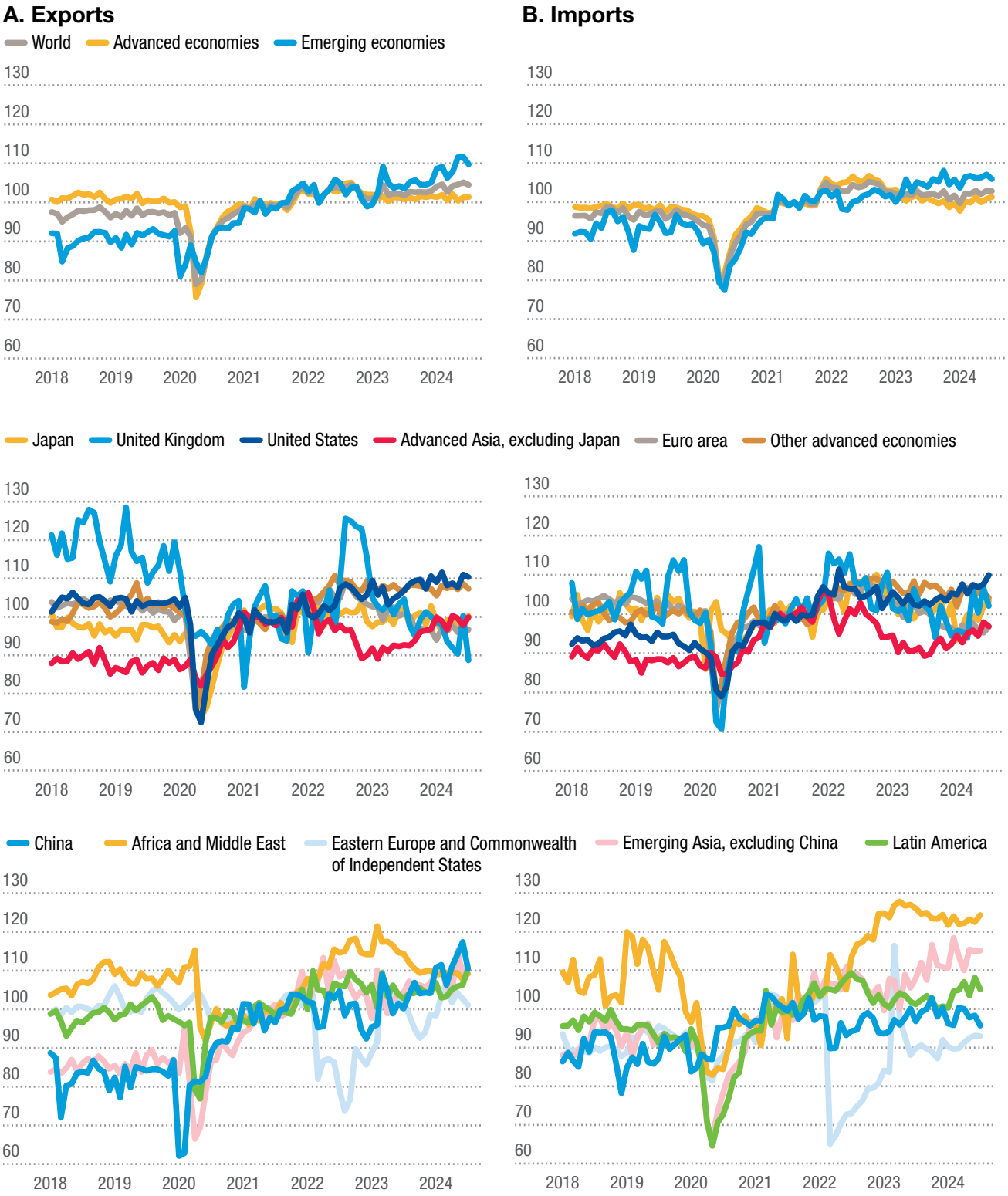
Two key factors suggest, however, that such buoyant export patterns may not continue through the second semester and plausibly also next year. One relates to front-loading orders from China and the risks of heightened trade tensions. The other links to the risk of an economic slowdown in the United States, in particular, and in the global economy as a whole.

With respect to front-loading orders from China, some analysts have suggested that this aspect has played a key role in stronger-than-expected Chinese export figures in the first half of 2024. This took place because economic agents expected new trade restrictions on the world's leading exporter of manufactures to kick in during 2024 (*Financial Times*, 2024f). In May 2024, the United States announced that it would hike tariffs on an array of imports from China, starting in August (United States, 2024). This includes quadrupling duties on Chinese electric vehicles to 100 per cent. While there is not necessarily a causal link, the record-high monthly trade surplus of $99 billion recorded by China in June 2024, when the Chinese economy was experiencing weak domestic demand and strong production capacity, might have been another element that exacerbated trade tensions.

The trade restrictions enacted in the United States were followed by similar measures by the world's major markets. For instance, the European Union confirmed in July that it would impose tariffs on electric vehicles, albeit only up to 37.6 per cent. Türkiye announced it would implement a 40 per cent additional tariff on Chinese-made electric vehicles. In late August, the Department of Finance of Canada decided on "implementing measures to protect Canadian workers and key economic sectors from unfair Chinese trade practices", which will become effective in October 2024 (Canada, 2024).

The adoption of increased protectionist actions was not restricted to OECD economies. Within developing Asia, Indonesia announced in July its intentions to impose import duties of up to 200 per cent on textile products, which come mainly from China (Reuters, 2024). India recently imposed a series of anti-dumping measures, and some observers have

Figure II.1
World merchandise is growing again, although divergences exist across regions
Trade flows in real terms, January 2018–July 2024
(Average 2021=100)



Source: The World Trade Monitor database of the CPB Netherlands Bureau for Economic Policy Analysis.

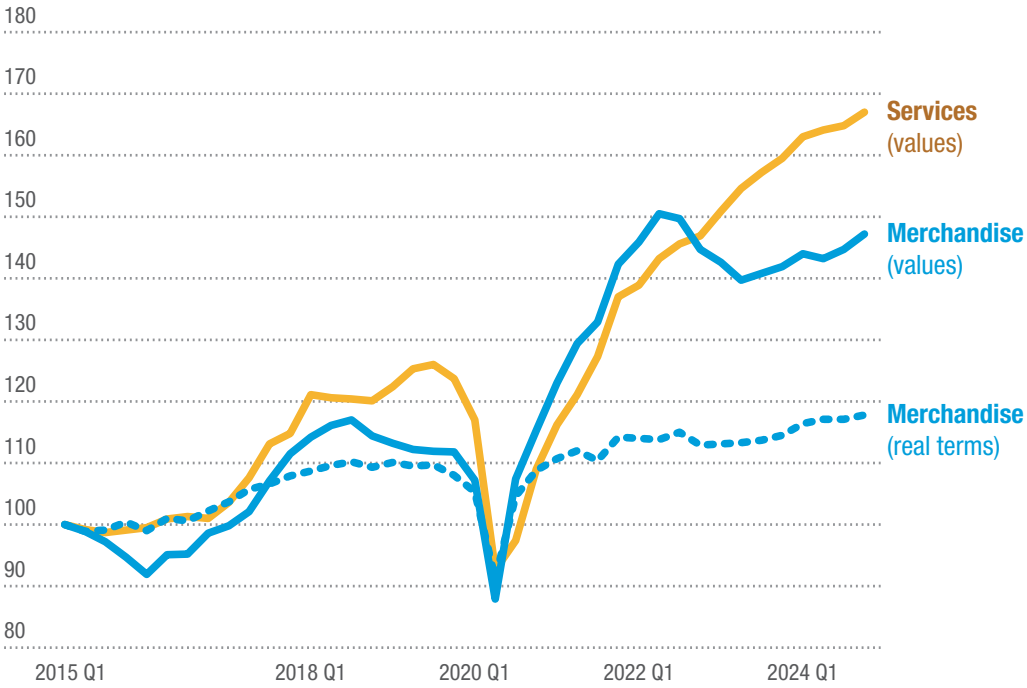
Note: Country group classification relies on CPB Netherlands Bureau for Economic Policy Analysis (see Ebregt, 2020).

reported a growing debate within the Government of India about whether or not to consider further restrictions on Chinese products and inward investments. Bilateral trade imbalances are deteriorating between the two economies, and India aspires to position itself as the "China plus one" manufacturing destination (*Financial Times,* 2024a). Thailand recently established a new Government body to examine restrictions on Chinese imports (Foreign Policy, 2024). In Latin America, Chile imposed anti-dumping tariffs on Chinese steel. Brazil and Mexico took similar measures.

In terms of economic deceleration, consumer spending had started to show signs of flagging in the United States after helping to prop up the world's largest economy since the pandemic. Given the fact that the United States has provided the most demand-side impetus – together with several large developing economies of East, South and South-East Asia, except China, which had contributed negatively to world imports by mid-2024 – further headwinds are expected during the second half of 2024.

Overall, signs of weaker prospects for merchandise trade in the quarters ahead had already appeared in several leading indicators. The July release of the global manufacturing Purchasing Managers' Index data, for instance, depicted a second consecutive monthly contraction for the new export orders component (S&P Global, 2024). The UNCTAD trade nowcast of September pointed to a growth deceleration from the second quarter of 2024 onwards (figure II.2).

Figure II.2
Trade in services continues to show more dynamism than merchandise trade
Quarterly world trade of merchandise and services, first quarter of 2015–fourth quarter of 2024
(First quarter of 2015=100)



Source: UNCTAD based on UNCTADstat database.

Notes: Q1, first quarter. All series are seasonally adjusted. Estimates from UNCTAD Nowcasts for the second to fourth quarters of 2024.

Trade in services remains more dynamic

In line with earlier dynamics, the outlook for trade in services remains comparatively better than for merchandise trade in 2024. Data for the first quarter show that world services exports in dollar terms increased by 9 per cent on a quarter-on-quarter, seasonally adjusted annualized-rate basis. High carbon emissions-intensive services grew most rapidly: travel expanded 18 per cent, while transport increased 15 per cent. All other commercial services grew 5 per cent.

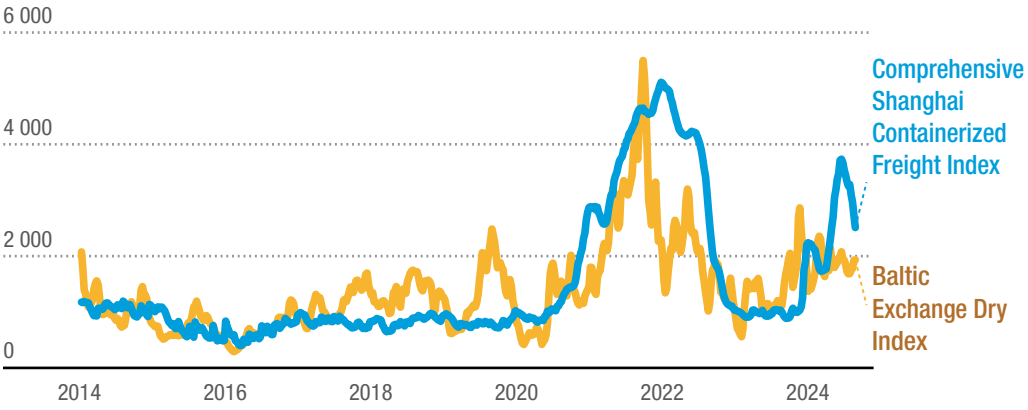
This expansion, however, hides a darker side: the heavy environmental footprint of current dynamism in transportation sectors. In maritime transport, increased revenues as of September 2024 partly resulted from the need to use longer trade routes, often at faster speed, to complete shipments between two given points (UNCTAD, 2024f). This was due to attacks on vessels in the Red Sea, and led to increases in both shipping costs and carbon dioxide emissions.

Regionally, preliminary data for the first quarter of 2024 suggests growth in services exports as a whole in Asia and Oceania, Northern America and Europe, at around 8 to 10 per cent on a quarter-on-quarter, seasonally adjusted annualized-rate basis. In Latin America and the Caribbean, growth reached 19 per cent on the back of robust performance in international transport services from Mexico.

For the rest of 2024, from the second quarter onwards, UNCTAD nowcast data for trade in services in dollar terms points to a continued expansion, ranging from 2 to 5 per cent on a quarter-on-quarter, seasonally adjusted annualized-rate basis, significantly below the rate during the first quarter. Forecasts point to an annual expansion of revenues of services exports of almost 6 per cent, while for merchandise, the corresponding figure will be just slightly more than 2 per cent.

Transport revenues are expected to rebound sharply over the course of 2024 due to significant price increases, particularly for container freight rates (figure II.3). This is due primarily to firmer demand as well as the disrupted routes in the Red Sea, and

Figure II.3
Container freight rates normalized in 2023 before surging again in 2024
Weekly Baltic Exchange Dry Index and Comprehensive Shanghai Containerized Freight Index (Base date=1,000)



Source: UNCTAD based on Clarksons Shipping Intelligence Network.

Note: The base date when the index number equalled 1,000 was 4 January 1985 for the Baltic Exchange Dry Index and 16 October 2009 for the Comprehensive Shanghai Containerized Freight Index. The two depicted series end in September 2024.

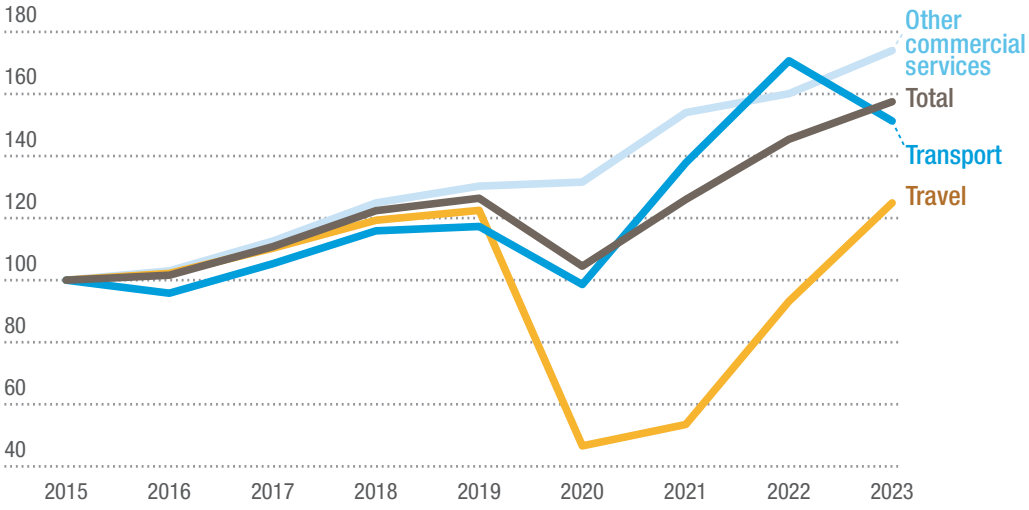
to a lesser extent to delays at the Panama Canal earlier in 2024 (UNCTAD, 2024f).

Regarding travel, about 790 million international tourists were registered between January and July 2024, some 11 per cent more than in 2023, though 4 per cent less than in 2019. Strong demand in Europe and the reopening of several markets in Asia and the Pacific supported this catch-up. Data show a strong start to the year, followed by a more modest second quarter. The United Nations Tourism Confidence Index of September 2024 suggests positive expectations for the last part of the year, at 120 points for September to December 2024, although this is below prospects for May through August, which stood at 130 (on a scale of 0 to 200, where 100 reflects equal expected performance). Overall, the number of arrivals for 2024 as a whole roughly match the record high in 2019. In international tourism receipts, 47 out of 63 countries with available data recovered pre-pandemic values during the first half of 2024, with many reporting strong double-digit growth compared to 2019, in local currencies and current prices (UNWTO, 2024).

In total, other commercial services are expected to grow roughly in line with trade in services in 2024. This diverse grouping of activities is dominated by business services, telecommunications and computer services, intellectual property, and insurance and financial services, and further comprises construction and personal, cultural and recreational services. Among these, telecommunications and computer services as well as financial services have experienced relatively faster growth.

Looking back, services trade recorded a robust expansion in 2023, with revenue growth of about 9 per cent in the global commercial services trade, computed as the average growth rate between exports and imports. In Latin America and the Caribbean, services trade expanded 13 per cent. For the limited number of African economies with data, it grew 11 per cent. These were the fastest-growing regions. Except for current and former members

Figure II.4
Growth in commercial services remains firm while the travel segment is still catching up
World exports of commercial services, selected components (2015=100)



Source: UNCTADstat database.

Note: Other commercial services comprises goods-related services, construction, insurance and pension, financial services, intellectual property charges, telecommunications, computer and information services, other business services, and personal, cultural and recreational services.

of the Commonwealth of Independent States, whose exports of commercial services stagnated, all other major regions experienced growth ranging from 7 to 9 per cent in 2023 (WTO, 2024).

Growth composition in 2023 was supported by the continuing fast rebound in travel, with international travel receipts rising at an annual rate of 35 per cent. This contrasts with an 8 per cent decline in global transport, which was also reflected in a sharp but transitory decline in shipping rates that temporarily brought them back to pre-pandemic levels. Other commercial services, including goods-related services, grew on a par with the aggregate for all services. Commercial services accounted for the bulk of services at 57 per cent, followed by transport and travel, with each accounting for 20 per cent of total services in 2023. Goods-related services came in last at 3 per cent (figure II.4).

Looking forward, a strong revival of world trade is unlikely

Beyond the rebound in world trade and its expected deceleration during 2024, the prioritization of domestic issues and the pressing need to fulfil climate commitments[8] are prompting shifts in trade and industrial policies. Higher reliance on trade restrictions and inward-focused industrial strategies, especially by the largest economies, are expected to prevent a smooth functioning of international trade in general and some key sectors in particular, such as aluminium, semiconductors and steel. Sectoral slowdowns, however, do not always correspond with reduced trade flows globally, as the expected eight-year record high of steel exports from China in 2024 illustrates (*Financial Times*, 2024c).

The long-term slowdown of world merchandise trade and its ongoing reconfiguration (UNCTAD, 2023a) as well as significant breakthroughs in information and communications and digital technologies prompt a rethink of development pathways. Once preferred strategies for development in low- and middle-income nations – centred around manufacturing export-led growth to absorb a sizeable portion of unskilled workers, boost productivity and ultimately stimulate economic transformation – appear to be increasingly unable to deliver simultaneously on these fronts. This calls for a wider consideration of key components of development strategies today.

The next section reviews some issues pertinent to decision-makers.

2. The quest for quality jobs: The limits of services-led exports

Until not so long ago, the path to economic development in the global South was mainly associated with industrialization. Manufacturing exports were expected to serve as a powerful engine, particularly for small economies with a limited domestic market. The rationale was straightforward. By focusing on manufacturing, these countries could achieve economies of scale, enhance productivity and integrate more effectively into the global economy, while creating employment opportunities, including for relatively unskilled workers moving from rural areas to growing cities.

For many developing nations, a certain type of manufacturing export-led strategy – ideally reflecting a country's specific context and conditions – was presumed to drive the convergence towards the most advanced economies. The success stories of several East Asian economies provided a compelling blueprint, although it is highly misleading to ascribe these successes only to greater

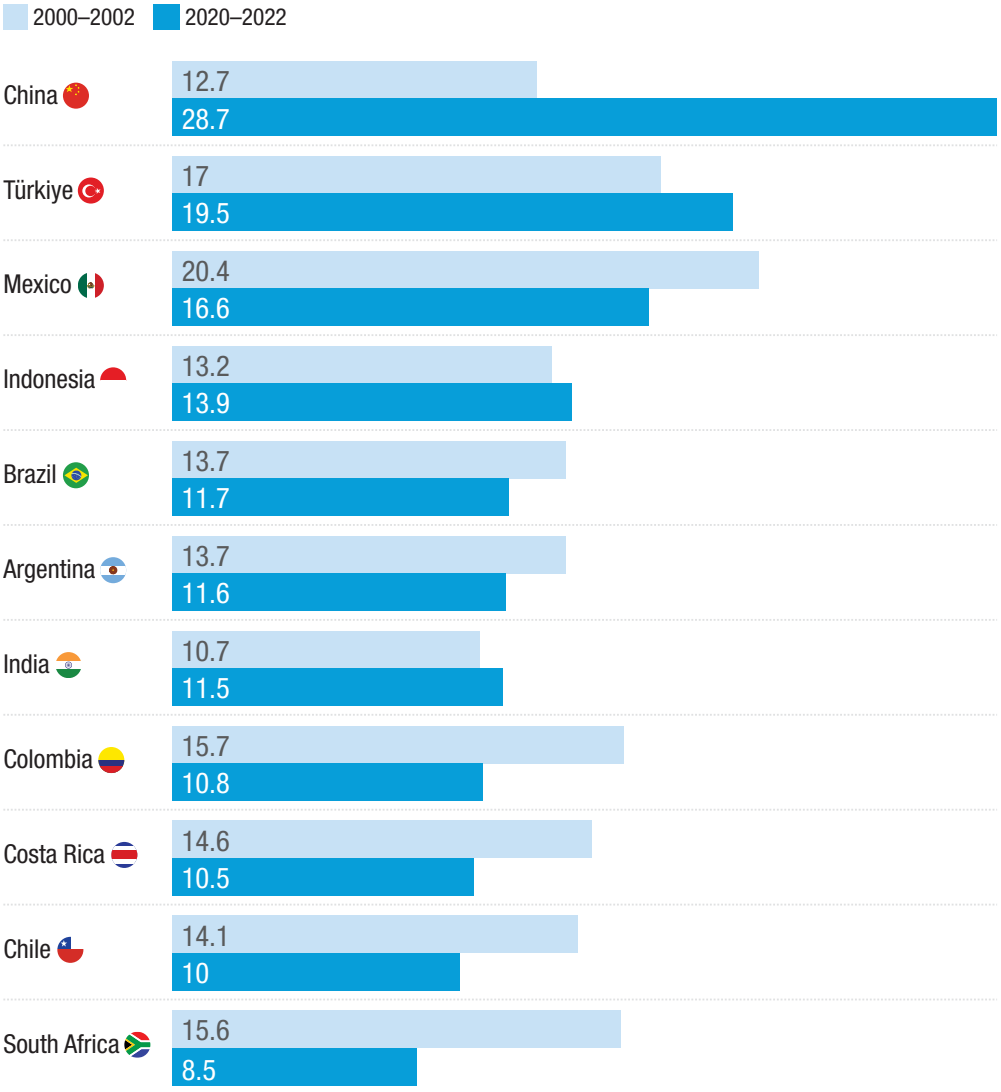
[8] The attempts to tackle climate change have remained insufficient to address global warming. Reducing carbon emissions by at least 45 per cent from 2010 levels by 2030 as well as reaching net zero around 2050 require immediate actions to phase out fossil fuel extraction, including from fossil fuel companies (United Nations Secretary-General, 2023).

trade openness. These countries deployed a combination of targeted industrial policies, investment in human capital and outward-oriented strategies that dramatically changed their economies (see chapter IV for further discussion on the limits of this model).

The global economic environment has evolved significantly since these economies embarked on their rapid transformations in the second part of the twentieth century. The lead of China in manufactures, the rise of industrial robots and digital technologies, shifts in global trade patterns and an increasing emphasis on sustainability have reshaped the contours of economic development, even though hardly any country has realistic plans for phasing out greenhouse gas emissions let alone preserving biodiversity. In terms of jobs provision, with few exceptions, many developing countries with significant industrial sectors have experienced declines in manufacturing as a share of total employment over the last two decades (figure II.5).

Figure II.5
Manufacturing employment has mostly declined in developing countries over the last two decades

Share of manufacturing employment in total employment, selected developing countries (Percentage)



Source: UNCTAD based on the Global Sustainable Development Goals Indicators Database of the United Nations.

While manufacturing remains important, there is growing recognition that the efficacy of industrialization as a growth strategy has been undermined. This is partly because the comparative advantage of developing countries – which still lies in the relative abundance of cheaper and less-skilled workers – no longer matches the skill- and capital-intensive production techniques that are increasingly central to many manufacturing processes. Further erosion of efficacy comes from the lack of attention to the heavy ecological and carbon footprint that industrialization and traded goods and services can generate (see box II.1). As research repeatedly confirms, the economic costs and physical damages imposed by accelerating climate change weigh primarily on developing countries and their poorest citizens (UNCTAD, 2022, 2023a).

Past studies identified the problem but fell short in defining required actions

Concerns about the limits of prevailing development strategies are not new. When it comes to structural transformation and the provision of jobs in developing countries, World Bank economists (Hallward-Driemeier and Nayyar, 2017), for instance, have raised concerns about the declining ability of manufacturing-led development to provide the dual benefits of productivity gains and job creation for unskilled workers. At the same time, they were nonetheless broadly positive about the benefits that manufacturing sectors and tradable services can offer if policymakers succeed in delivering on the "3 Cs", namely:

- Competitiveness. To develop firm ecosystems, shift from a focus on low wages to broader considerations of the business environment, the rule of law and the use of technology to complete financial transactions.
- Capabilities. Equip workers with new skills, build stronger firms and develop necessary infrastructure to adopt modern technologies.
- Connectedness. Improve logistics, lower trade restrictions on manufactured goods and lower trade restrictions on services.

Going one step further, Baldwin and Forslid (2023) anticipated that services-led development would become the norm rather than the exception in the future. Because success in the services sector relies on factors distinct from those in manufacturing, there is a moderate optimism regarding the potential of trade in services to raise the incomes of relatively high-skilled workers living in urban areas in middle-income countries. This is based on the assumption that services trade would allow developing nations to directly export the source of their comparative advantage – i.e. labour, which is low cost given its lower productivity – without having first to make goods with that labour and then export the goods. In other words, joining service value added chains would require less of a push than the development of an industrial base. Yet the accumulation of human capital may take longer, compared to the time needed to accumulate physical capital in a context of significant financial openness.

Using data from the Statistics on Trade in Value Added database of OECD and World Trade Organization (WTO), Baldwin (2024) defines an output-based indicator to capture when countries have experienced export-led growth episodes. Considering two time periods, 1995–2008 and 2008–2020, and three income-level groups, the study seeks to establish whether and when the value added in exports has grown faster than GDP, which can be computed for both manufacturing and services. Findings show that, among countries listed in the database of OECD and WTO, a majority of lower- and upper-middle-income countries experienced manufacturing export-led growth during 1995–2008. About 60 per cent of lower-middle-income countries and 80 per cent of upper-middle-income ones saw manufacturing exports grow faster than GDP at that time. Value added growth in tradable services was about 40 per cent in lower-middle-income countries and 50 per cent in upper-middle-income ones.

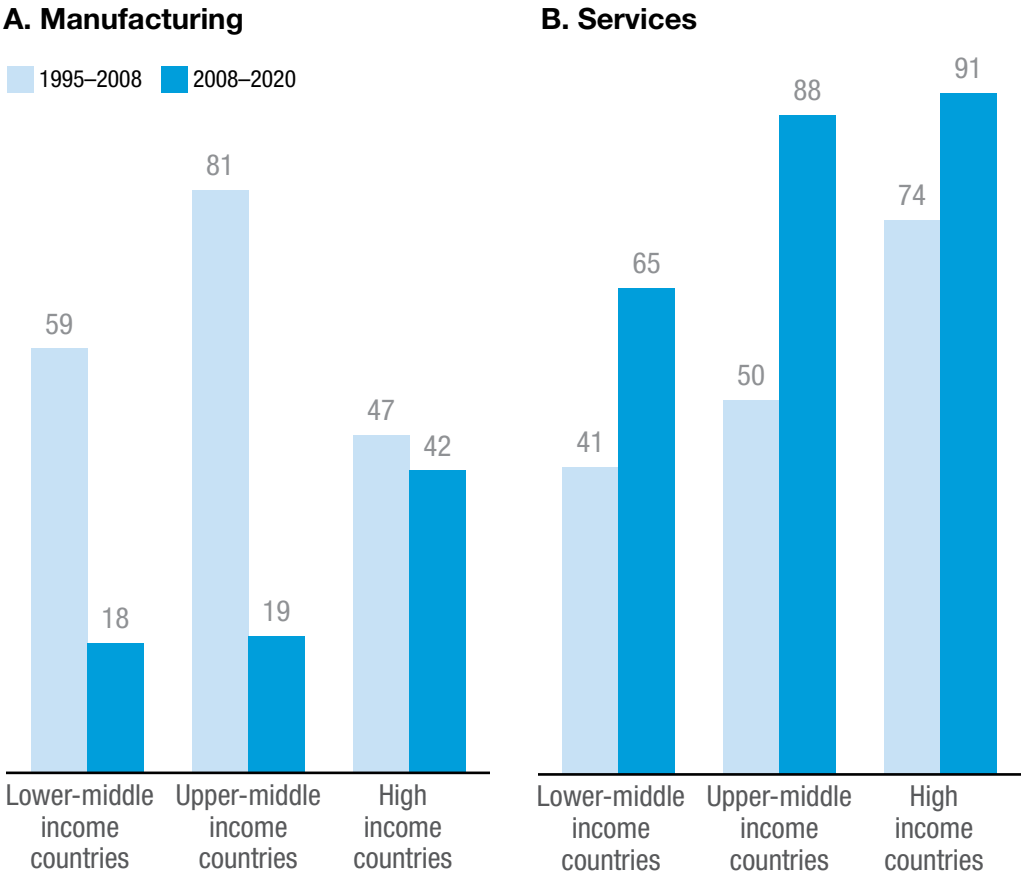
Manufacturing-led exports used to support growth in middle-income countries ahead of the global financial crisis.

Manufacturing-led export growth effectively dominated the picture in both groups in the decade before the global financial crisis.

Nowadays, services-led export growth is more likely.

In the aftermath of the global financial crisis, which made clear that previous global growth patterns were unsustainable, drastic changes occurred. Less than 20 per cent of middle-income countries still registered manufacturing-led export growth during 2008–2020, while almost 70 per cent of lower-middle-income countries and 90 per cent of upper-middle-income ones recorded services-led growth within these years. Interestingly, among high-income countries, the percentages registering manufacturing- and/or services-led growth have remained more stable, despite a slight decrease in manufacturing-led growth episodes and an uptick in services-led ones between the two time spans (figure II.6). This supports the view that manufacturing-led export growth is somehow losing steam while services-led growth is booming.

Figure II.6
Manufacturing-led export growth is declining while services-led export growth is booming
Share of economies experiencing manufacturing- and/or services-led export growth, selected income groups
(Percentage)



Source: Baldwin (2024).

Notes: This figure reports the percentage of countries within each income group that experienced export-led growth in manufacturing and services during the two considered periods. A country is considered as having export-led growth in one of the two sectors if the value added in sector exports grew faster than GDP. A country can register both types of export-led growth simultaneously. Services-led export growth only considers information and communications technology-enabled services trade and excludes transportation and tourism. The lower-middle-income country group contains 17 economies, the upper-middle-income one 16 and the high-income group comprises 43 economies.

Demand-side measures and modern industrial policies need to be expanded to all economic sectors

While studies present some compelling arguments about structural transformation, their policy recommendations are not really appropriate from a macro perspective. The menu of policy options suggested in Hallward-Driemeier and Nayyar (2017), for instance, mostly comprises supply-side measures and fails to acknowledge the fundamental role of modern industrial policies in fundamentally reorienting and expanding the demand side for both the overall economy and the labour market. Also, while equipping workers with new skills always looks promising, the proposed policies are of little relevance to the majority of unskilled workers who will not become skilled overnight. As such people constitute the bulk of the labour force in developing nations, especially ones with the lowest income per capita, a more comprehensive approach needs to be proposed.

In short, it will be crucial to put greater emphasis on tertiary sectors in general and non-traded ones in particular. Absent government policies that explicitly target the structural transformation of economic activity in pursuit of some public goal – the way Juhasz et al. (2019) define industrial policies – markets, left to their own dynamics, are unlikely to drive needed structural change (not to mention their inability to address burning ecological issues that most affect unskilled workers in poorer countries).

A strategic approach to modern industrial policies broadened to encompass all economic sectors, including services, is key to a climate-conscious developmental paradigm. Considering the discussion above, such an approach should also go beyond industrialization per se and consider the increasingly important interplay between environmental, demographic, financial and technological factors that affect economic growth, trade and global supply chains.

Trade in services alone faces several limitations and can scarcely be expected to become a realistic alternative to manufacturing-led development. It hardly fulfils the dual mandate of enhancing productivity gains and creating many jobs for unskilled workers, not to mention the growing negative environmental footprint of some activities (box II.1).

On the one hand, tradable services that are productively dynamic – such as banking, information technology and business-process outsourcing – provide limited scope to generate widespread employment for unskilled workers, for the same reason that manufacturing nowadays is unable to generate sufficient jobs for the unskilled labour force (see chapter IV for a discussion of the “finance curse”). In short, these sectors often rely primarily on high-level skills and automated processes. On the other hand, more labour-intensive sectors such as tourism and construction do not generate significant productivity enhancements given limited possibilities for achieving meaningful economies of scale and creating backward and forward linkages.

Modern industrial policy encompassing all economic sectors including services is needed.

Box II.1
On the growing energy use and carbon footprint of trade in services

The positive framing of trade in services for sustainable development partly relies on the assumption that services are more dematerialized and less harmful to the climate and environment than trade in manufacturing. Yet many services, such as transport and international travel, are highly carbon-intensive and hard to decarbonize. Digitally delivered services, such as e-commerce, are energy-intensive and generate strong rebound effects as they generally accelerate the production, circulation and consumption of material goods. The case for pitching the fast growth of trade in services – and even digital services – as a sustainable development path appears limited and questionable.

Digitally delivered services and trade across borders have grown very rapidly. Between 2005 and 2022, exports of digitally delivered services expanded by 375 per cent (World Bank and WTO, 2023). This boom would not have been possible without the rapid expansion of material supporting systems, such as information technology goods and infrastructure or "smart" devices. This aspect of digitally delivered services compounds the challenge of electronic waste, which is often exported from developed to developing countries, and is growing five times faster than reported e-recycling (WHO, 2023; UNITAR, 2024).

Cryptomining and data centres alone accounted for 2 per cent of global electricity use and nearly 1 per cent of global emissions in 2022.

Moreover, this boom would not have been possible without growing water and energy use. According to some studies, the energy consumption of the information and communications technology sector has grown by 9 per cent per year on average during the last decade. Its share in global carbon emissions increased from 2.5 per cent in 2013 to 3.7 per cent in 2018 and may reach 8 per cent by 2025 (The Shift Project, 2018). Cryptomining and data centres alone accounted for 2 per cent of global electricity use and nearly 1 per cent of global emissions in 2022, and their footprint is growing fast. One bitcoin transaction requires roughly the same amount of electricity as the average person in Ghana consumes in three years or the average person in Germany in three months. ChatGPT queries require 10 times more electricity than a Google search, due to the electricity consumed by artificial intelligence data centres (Hebous and Vernon-Lin, 2024a, 2024b).

Dashing hopes of a "weightless" digital economy, the exponential growth of digitally delivered services instead undermines the possibility of cutting global carbon emissions by 95 per cent by 2050, as envisioned in net-zero climate scenarios (Pitron, 2021). Consequently, and amid fallacious net-zero claims, big technology companies are missing their climate targets by large and increasing margins. Because reducing emissions while growing at such rapid rates remains impossible, these firms have instead led attempts to gut science-based carbon metrics and rewrite carbon accounting rules (*Financial Times*, 2024f, 2024g).

As underscored by UNCTAD (2024a), developing countries experience most of the environmental costs of digitalization while reaping fewer benefits. They export low value added raw materials and import high value added devices, along with increasing digital waste. Such challenges call for a cautious approach to increased trade in digitally delivered services as an avenue to reach sustainable development. To move away from this unsustainable model, a global shift towards sufficiency, including in the digital sector, and enhanced efforts to promote circularity are required.

Sources: Hebous and Vernon-Lin (2024a, 2024b); *Financial Times* (2024d, 2024g); Pitron (2021); The Shift Project (2018); UNCTAD (2024a); UNITAR (2024); WHO (2023); World Bank and WTO (2023).

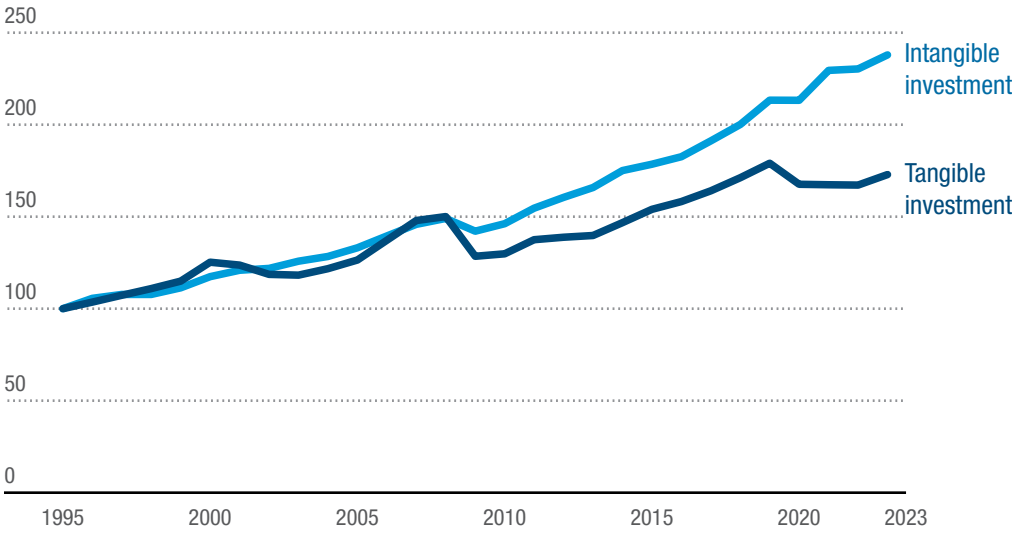
Furthermore, information and communications technology-enabled services, or even trade in services in general, usually remain primarily dominated by developed countries. Recent trade data show a low number of non-high-income developing economies in the top 30 economies in world services exports in 2023. This contrasts with merchandise trade, for which the figure is larger. In aggregate, developing economies accounted for less than 30 per cent of world services export revenues; the figure for merchandise exports is 44 per cent (table II.1).

The growing role of intangible assets adds to these concerns (figure II.7). According to the Asian Development Bank (ADB) et al. (2021: xviii): "Conventional trade statistics do not capture exports in the services of intangibles via [global value chains and therefore they] substantially underestimate the actual exports of developed economies and distort the trade balance between them and developing economies". Yet intangible assets, such as brands, unique designs, patented technologies and the knowledge of supply chain management, rather than tangible assets (i.e. manufacturing production), are increasingly determining the ability of firms to lead and benefit from global value chains. In the extreme, this may lead to "factory-less" production in which firms that design and market manufactured products own none of the production process. As a result, an important part of modern global value chains consists of innovator countries exporting the services of their intellectual property in return for manufactured goods (ADB et al., 2021: xi).

According to the World Intellectual Property Organization (WIPO) and Luiss Business School (2024), investment in intangible assets such as brands, designs, data and software has grown three times faster over the past 15 years than investment in physical assets such as factories and machinery. France, Sweden and the United States have seen the most intensive activity, and India is trending upward. In 2023, aggregate intangible investment touched $6.9 trillion, more than doubling from $2.9 trillion in 1995. Tangible investment rose to $4.7 trillion in 2023.

Developing countries represented less than 30 per cent of world services export revenues and 44 per cent of merchandise exports in 2023.

Figure II.7
The ability of firms to lead and benefit from global value chains increasingly relies on intangibles
Intangible and tangible investment in the world
(1995=100)



Source: WIPO and Luiss Business School (2024).

Table II.1
Top 30 rankings in world commercial services and merchandise exports in 2023

	COMMERCIAL SERVICES			MERCHANDISE		
Rank	**Economies**	**Percentage**	**Billions of dollars**	**Economies**	**Percentage**	**Billions of dollars**
1	United States	13.0	1 027	China	14.2	3 380
2	United Kingdom	7.4	584	United States	8.5	2 020
3	Germany	5.5	439	Germany	7.1	1 688
4	Ireland	5.0	398	Netherlands (Kingdom of the)	3.9	935
5	China	4.8	381	Japan	3.0	717
6	France	4.6	360	Italy	2.8	677
7	India	4.3	338	France	2.7	648
8	Singapore	4.1	328	Republic of Korea	2.7	632
9	Netherlands (Kingdom of the)	3.9	312	Mexico	2.5	593
10	Japan	2.6	207	Hong Kong (China)	2.4	574
11	Spain	2.5	198	Canada	2.4	569
12	Switzerland	2.1	169	Belgium	2.4	562
13	United Arab Emirates	2.1	166	United Kingdom	2.2	521
14	Luxembourg	1.9	149	United Arab Emirates	2.1	488
15	Italy	1.9	148	Singapore	2.0	476
16	Belgium	1.8	146	Taiwan Province of China	1.8	432
17	Canada	1.7	137	India	1.8	432
18	Republic of Korea	1.6	124	Russian Federation	1.8	424
19	Denmark	1.4	114	Spain	1.8	423
20	Poland	1.4	108	Switzerland, Liechtenstein	1.8	420
21	Sweden	1.3	104	Poland	1.6	382
22	Türkiye	1.3	102	Australia	1.6	371
23	Hong Kong (China)	1.2	98	Viet Nam	1.5	354
24	Austria	1.1	90	Brazil	1.4	340
25	Israel	1.1	83	Saudi Arabia	1.4	322
26	Australia	0.9	74	Malaysia	1.3	313
27	Thailand	0.7	57	Thailand	1.2	285
28	Portugal	0.7	56	Indonesia	1.1	259
29	Taiwan Province of China	0.7	54	Türkiye	1.1	256
30	Greece	0.7	53	Czechia	1.1	255
	World	**100.0**	**7 913**	**World**	**100.0**	**23 784**
	Developing economies	29.7	2 348	Developing economies	44.1	10 489
	Developed economies	70.3	5 566	Developed economies	55.9	13 295

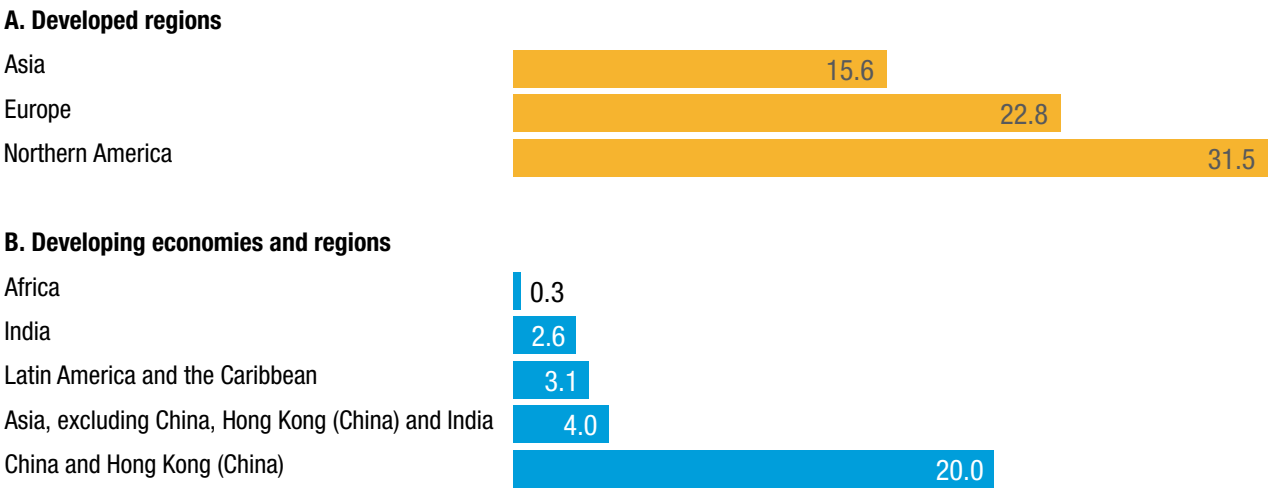
Source: UNCTADstat database.

Besides concerns relating to intangible assets, issues about market concentration, such as in the creative services trade,[9] also show how developed economies continue to lead in an area that is often portrayed as a plausible multifaceted engine for economic development. While the value of this sector rose to $1.4 trillion in 2022, developed economies still accounted for 80 per cent of exports in 2022. This contrasts with the size of developed countries in the world economy, which is less than 60 per cent.

High concentration is also reflected in the geography of headquarters of large multinational enterprises providing international services. As figure II.8 shows, 70 per cent of headquarters activities in international trade in services are in advanced regions, compared to only 10 per cent for the rest of the developing world outside China, including Hong Kong Special Administrative Region (SAR). This figure was derived from the financial statements of a group of almost 1,000 multinational enterprises, both publicly traded and not, that each recorded more than $10 billion in revenues in 2022. Arguably, these are key players in international services with their revenues, albeit also from domestic activities, collectively accounting for almost $35 trillion in 2022, more than five times the value of trade in services that year.

Figure II.8
Headquarters of major multinationals responsible for most trade in services are mostly located in developed regions and China

Share of headquarters locations of large multinational enterprises providing international services
(Percentage)



Source: UNCTAD based on LSEG Eikon.

Notes: The sample refers to 924 companies, both publicly traded and not, that each had more than $10 billion in revenues from goods and services sold in 2022, and whose activities involve the international trade of services (i.e. excluding companies primarily involved in the production and export of goods). School (2024).

[9] Creative services trade statistics cover the following categories of services: advertising; market research; architecture; audiovisual; cultural; recreational; heritage-related; information; research and development; and software.

Although interesting export promotion initiatives have emerged recently in trade in services, tradable services will remain insufficient to absorb a major part of the labour force in developing countries (UNCTAD, 2024i). More broadly, asymmetries in exports among country groups – together with issues of market concentration and competition-related concerns as recently reassessed by UNCTAD (2024d) – explain why it seems difficult to envisage that international services could supersede what manufacturing-led development successfully achieved in some parts of the developing world in the past. Deductive reasoning suggests that there is no other solution than turning to services in some non-tradable sectors, a topic addressed in the remaining part of this section.

An ambitious policy mix in non-tradable sectors will be necessary

Recognizing the inability of trade in services to provide enough quality jobs to the majority of underemployed people in developing countries, Rodrik and Stiglitz (2024) recently proposed a more radical policy shift centred on the green transition and the promotion of labour-absorbing services activities, mostly in the non-tradable sectors. They advocate a three-pronged strategy based on:

- Encouraging lower-skill job creation by larger firms in non-tradable services
- Providing public inputs and access to productivity-enhancing investments for smaller enterprises
- Investing in technologies that complement rather than replace low-skilled workers in services sectors.

This strategy argues for more inclusive and equitable growth strategies even if growth is lower. In short, it is about quality rather than quantity. The core idea is to deliver direct income gains for poorer segments of society through better jobs and, thus, to build a middle class, rather than wait for a "trickle-down" from the export champions and largest firms.

New studies have been advancing a vision for services-led economic development in more practical terms, even if there is still a long way to go before understanding well how to raise productivity in labour-absorbing services. Rodrik and Sandhu (2024), for instance, sketch four strategies that could be explored – and are not mutually exclusive – to expand productive employment in services that create the most jobs in developing countries, drawing from concrete examples in India, Nigeria and South Africa (table II.2).

Effective strategies for expanding employment opportunities in the services sector must be selective, targeting firms and subsectors with higher chances of success. Experimentation is essential and more likely to work when decentralized. This is because local governments, such as municipalities and subnational authorities, are often more aware of specific local conditions. Hence, they may be best suited to conduct and implement pilot programmes.

An important dimension is to enhance employment prospects for those at the lower end of income distribution. This is likely to boost the middle class and further stimulate domestic demand, which could support a virtuous cycle reinforcing economic growth, social inclusion and job creation.

For the natural environment not to be the poor relation of these future growth strategies, authorities, in selecting targeted sectors and firms, should consider expected linkages that planned developments will trigger in both economic and environmental terms. Absent such consideration, long-lasting and plausibly increasing costs are likely. These could ultimately exceed the benefits of such interventions.

As policymakers embark on the challenging journey of critically reviewing, assessing and plausibly recalibrating development pathways for the decades to come, the discussions above can provide some valuable food for thought. At this juncture,

it is worth stressing that perhaps the most cautious and promising approach to implementing modern industrial policies involves two aspects in parallel: Addressing the identified problem while minimizing adverse effects on international cooperation and multilateralism. This new odyssey will not be easy, as was the case for previous attempts to harness the best of globalization. Boosting productivity in services is known for being complicated. Yet attempts to provide good jobs for most citizens without greater consideration of non-tradable services seem increasingly implausible.

Table II.2
Four strategies for expanding productive employment in labour-absorbing services

Focus	Actions	Expected benefits	Illustrative case
▶ Established large and relatively productive incumbent firms	Incentivizing such firms to expand their employment either directly or through local supply chains	Generating upstream linkages with service providers	Saksham Saarthi Partnership with Uber and Ola in Haryana, India
▶ Small enterprises	Providing such firms with specific inputs (e.g. management training, loans or grants, customized skills among workers, specific infrastructure or technology assistance)	Enhancing productive capabilities in such firms	Youth Enterprise with Innovation (YouWiN!) in Nigeria
▶ Workers or firms	Offering digital tools and other modern technologies that explicitly complement low-skill labour	Enabling less educated workers to do (some of) the jobs traditionally reserved for more skilled professionals and increasing the range of tasks they can perform	The Manthan Project in Uttar Pradesh, India
▶ Less-educated workers	Combining vocational training with "wrap-around" services, a range of additional assistance programmes for job seekers	Enhancing the employability, retention and eventual promotion of less-educated workers	Harambee Youth Employment Accelerator in South Africa

Source: UNCTAD based on Rodrik and Sandhu (2024).
Note: Saksham saarthi translates to "capable charioteer/driver".

C. Commodity markets: Prices have receded but remain high

Commodity prices remained elevated as of July 2024. Although they have declined compared to the heights they reached following the outbreak of the war in Ukraine, aggregate commodity prices remain more than 20 per cent above their 2019 level.

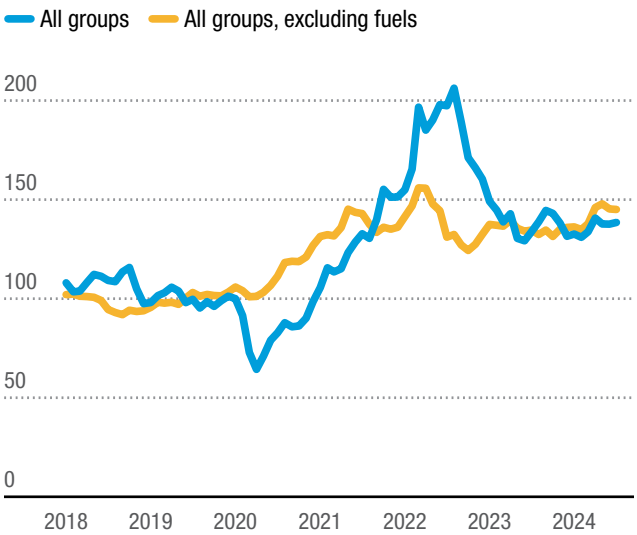
During the first months of 2024, non-fuel commodity prices rose. Fuel prices declined slightly during the second quarter amid decelerating demand worldwide (figure II.9).

These developments occurred after some volatility in 2023. The UNCTAD commodity price index for all commodity groups saw a notable 12 per cent increase from June to September 2023, attributed to a surge in fuel prices resulting from supply cuts announced by the Organization of Petroleum Exporting Countries and its allies (OPEC+). A subsequent decrease of approximately the same magnitude happened from September to December 2023, leaving the overall annual average way below the one recorded in 2022.

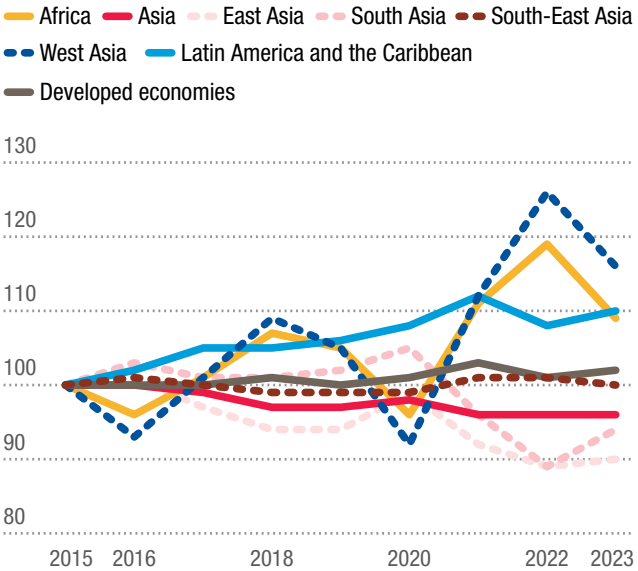
Consequently, the net barter terms of trade of the main commodity-exporting regions deteriorated slightly from 2022 to 2023,

Figure II.9
Commodity prices softened but remained more than 20 per cent above pre-COVID-19 levels

A. UNCTAD commodity price index
(Average 2019=100)



B. Net barter terms of trade, selected country groups
(2015=100)



Source: UNCTAD based on UNCTADstat database.

Note: In panel A, data ends in August 2024.

although not enough to offset gains made in recent years. Africa and Western Asia, for instance, experienced a decline of almost 10 per cent of their terms of trade. Individual countries had greater deteriorations, such as Angola (23 per cent), Equatorial Guinea (35 per cent) and Nigeria (14 per cent).

Aggregate commodity prices are anticipated to increase slightly. Announced and expected monetary easing in advanced economies will likely support such an evolution. Rising demand for critical energy transition minerals, particularly from China, will support aggregate commodity prices (see chapter III for an in-depth discussion). At the same time, the ongoing war in Ukraine and situation in Gaza may threaten the supply of commodities travelling through maritime trade routes, such as the Black Sea and Red Sea, and generate price volatility.

1. Oil and natural gas: High profitability limits the energy transition

Fossil fuel commodity prices were volatile during recent economic downturns and crises. The price of natural gas increased more than tenfold between the trough of June 2020 caused by the COVID-19 pandemic and the peak of August 2022 after the outbreak of war in Ukraine. Yet both oil and natural gas prices have since returned to levels below those prevailing prior to February 2022. Oil prices have stabilized and fluctuated mostly above $80 per barrel over the past 12 months (figure II.10.A), benefitting fossil fuel exporters and weakening incentives to diversify away from oil-export dependency (see table III.1).

Demand for fossil fuels has historically grown in tandem with global economic activity. As climate action and emissions mitigation remain dangerously insufficient, the share of fossil fuels in the primary energy mix has remained constant at around 80 per cent, independent of fossil fuel price swings over the years (figure II.10.C and D). The few temporary drops in global oil consumption, such as in 2009 and 2020, were not caused by high oil prices but by severe global economic downturns weighing negatively on economic activity and energy demand. It appears unlikely that higher fossil fuel prices and markets alone will be enough to phase out fossil fuels on the road to net zero (*Financial Times,* 2024g). This tendency is accentuated by continuing fossil fuel subsidies (UNCTAD, 2023a).

Fossil fuels have accounted for 80% of global primary energy since 1965, independently of price swings over the years.

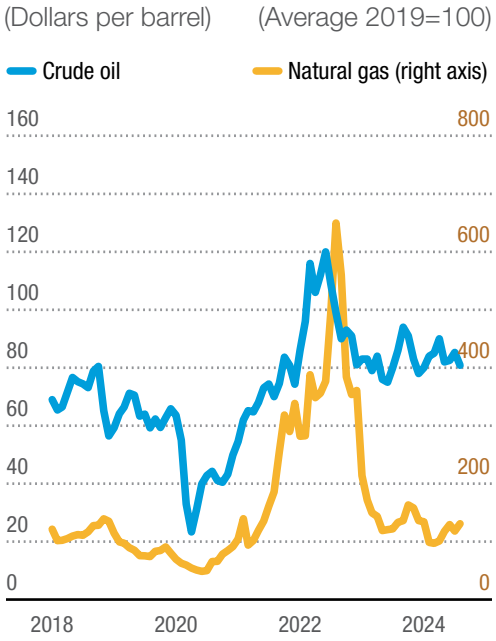
As energy consumption is largely captive to and dependent on long-term infrastructure investment decisions made by energy suppliers, expected profit in the fossil fuel sector appears to be the most significant determinant of future fossil fuel extraction. The profitability of fossil fuels remains higher than that of renewable energy (figure II.10.B). Although renewable energy consumer prices will continue declining, this trend alone is unlikely to much affect prevailing high profitability and output in the fossil fuel sector (Christophers, 2022, 2024).

In this regard, the International Energy Agency (IEA) and OPEC hold contrasting views. While the former claims that fossil fuel demand is set to peak in 2030, notably because of growing "green" investment and a rising supply of cheaper renewable energy (IEA, 2023), the latter argues that "peak oil demand is not on the horizon". OPEC (2024) instead expects fossil fuel extraction to keep rising to at least 116 million barrels per day by 2045, up from 102 million barrels per day in 2023. In the short term, and in the absence of binding quantitative regulatory limits on fossil fuels extraction and trade, both IEA and OPEC project oil consumption will rise as usual by 1 million to 2 million barrels per day in 2024.

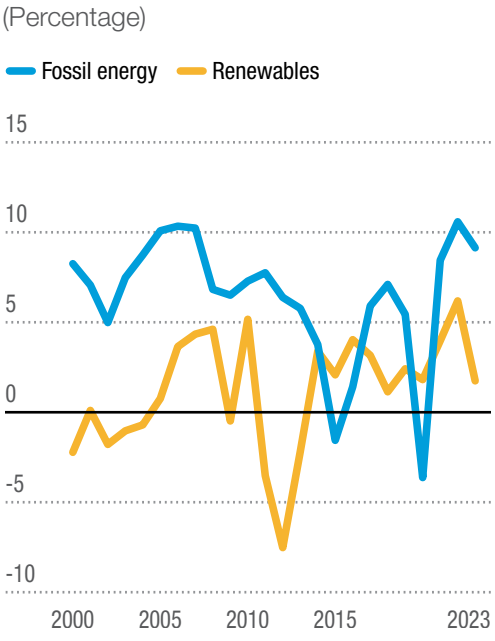
The profitability of fossil fuels continues to push net-zero goals far out of reach.

Figure II.10
Global fossil fuels are historically profitable and rising, regardless of price swings

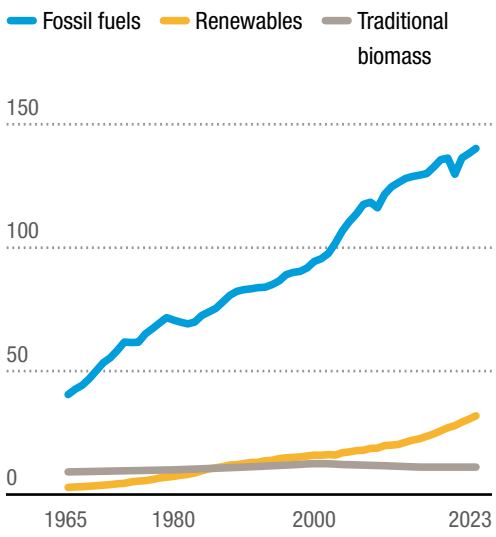
A. Oil and natural gas prices



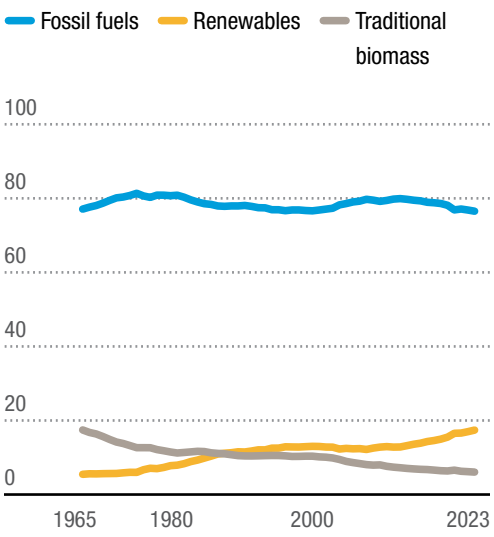
B. Ratio of profit to revenues in the energy sector



C. Primary energy consumption, by type



D. Share in primary energy, by type



Source: UNCTAD based on UNCTADstat database, LSEG Eikon and the Commodities Price Data (The Pink Sheet) of the World Bank.

Notes: In panel A data ends in August 2024. Primary energy consumption data in panels C and D are based on categorizing "fossil fuels" as including oil, gas and coal, and "renewables" as including hydropower, nuclear, wind, solar, modern biofuels and other renewables. Financial data on profit and revenues in panel B define nuclear as a separate category that is not included under "renewables".

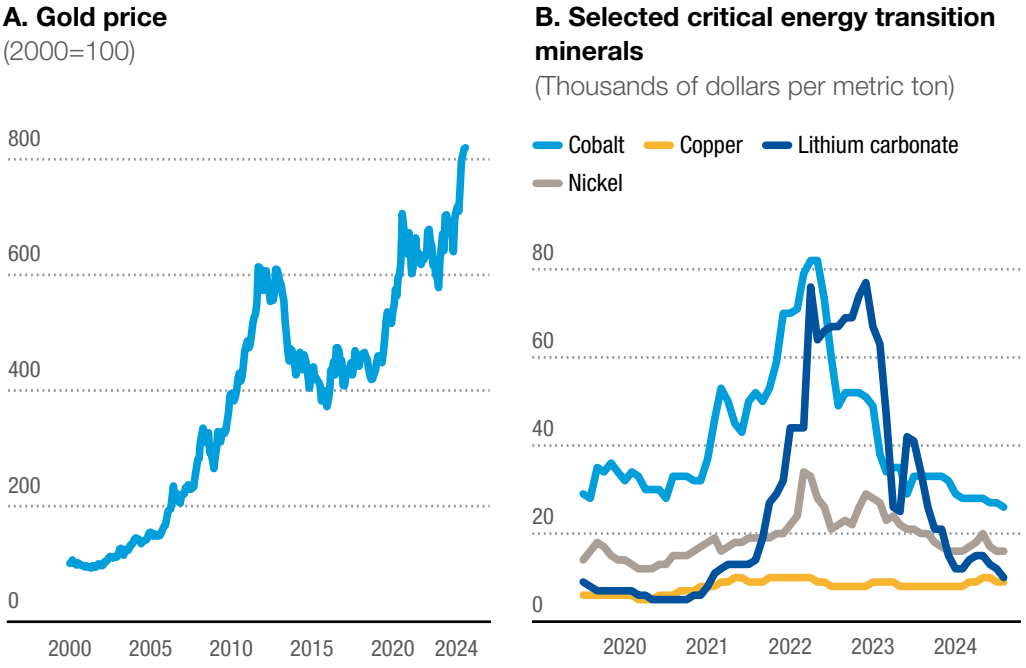
2. Minerals and metals: Price volatility remains amid intensifying geostrategic competition

Much like other aggregate commodity indices, the UNCTAD minerals, ores and non-precious metals index has been less volatile since early 2023 compared to previous years. It experienced an 11 per cent decline between February and May 2023, reflecting falling prices across key commodities such as aluminium, copper, iron ore and nickel. Following relative stability from June to December 2023, the index has risen again by more than 10 per cent since February 2024.

Precious metals such as gold and platinum experienced comparable price trends. The price of gold in particular rose by 25 per cent between March and mid-September 2024. It reached a new record high (figure II.11) on the back of strong demand from customers but also from central banks of countries planning to reduce their reliance on the dollar, such as China, India, Kazakhstan and the Russian Federation. The rising price of gold also reflected market expectations of imminent monetary easing in the United States, which stoked fears of resurging inflation and dollar depreciation, even though massive quantitative easing in past decades has shown that such expectations might be misguided.

Price volatility has been most acute in markets for some critical energy transition minerals. Lithium, cobalt and nickel prices fell by 78 per cent, 34 per cent and 42 per cent, respectively, in 2023 (figure II.11). The decline was partly due to a surge in production and an oversupply of these raw materials, following strong demand for electric vehicles and batteries in 2021 and early 2022. Additionally, slow growth in electric vehicle battery sales, coupled with large-scale production of battery cells and cathodes, led to a significant build-up of downstream products in inventory.

Figure II.11
Critical energy transition minerals and gold prices are highly responsive to geopolitical tensions and supply bottlenecks



Source: UNCTAD based on United States Federal Reserve Economic Data, LSEG Eikon and the Commodities Price Data (The Pink Sheet) of the World Bank.

Note: Data ends in August 2024.

Chinese manufacturing fluctuations cause higher price volatility for critical energy transition minerals than for other minerals.

China commands half of global demand for this group of metals and minerals. Given its outsized market share in the production of electric vehicles (58 per cent), wind turbines (66 per cent), and lithium batteries and solar panels (more than 80 per cent each), the prices of critical energy transition minerals are even more dependent than other metals and minerals on fluctuations in manufacturing in China.

In a context of price volatility and intensifying geostrategic competition for critical energy transition minerals, a growing number of countries importing them have attempted to secure a stable and diversified supply through trade-related agreements. In 2023, 22 such agreements were signed. Producing countries, such as Indonesia, Malaysia, Namibia and Zimbabwe, have adopted export-restricting measures to leverage mineral resources for domestic industrialization, enabling the capture of a larger share of value added compared to continued raw material exports (UNCTAD, 2024e). Such trends may persist and contribute to tightening markets for critical energy transition minerals, generating renewed upward price pressures.

3. Food and fertilizers: Elevated prices still weigh on poor households

Food commodity prices can have the most destabilizing short-term impacts on developing nations. In 2023, food commodity prices remained elevated, adding to the import bills of food-importing developing countries. It was only in December 2023 that the UNCTAD food index declined below its February 2022 level, stabilizing at about 20 per cent above its pre-pandemic level.

The prices of other agricultural commodities, such as vegetable oilseeds and oils prices, experienced similar fluctuations. By contrast, prices of tropical beverages have risen sharply since the beginning of 2024, owing to negative weather conditions and climate phenomenon, such as El Niño, that affected agricultural production.

Prices of fertilizers have also stabilized above pre-pandemic levels (figure II.12). The prices of potassium and urea reached unprecedented highs following the outbreak of the war in Ukraine and have declined since then. By contrast, the price of phosphate rock fell only in November 2023 by about 50 per cent, based on improved production prospects driven mainly by lower input costs, before stabilizing above its pre-pandemic level.

Among major food commodities, the prices of cereals such as maize and wheat have slowly declined since early 2023, returning closer to their pre-pandemic levels (figure II.12). The Black Sea Initiative, although it was suspended in July 2023, enabled a sharp decline initially as it contributed to continued Ukrainian agricultural exports and improved production and exports from the Russian Federation, which increased from 76 to 104 million metric tons from 2021–2022 to 2022–2023, according to the Agricultural Market Information System.

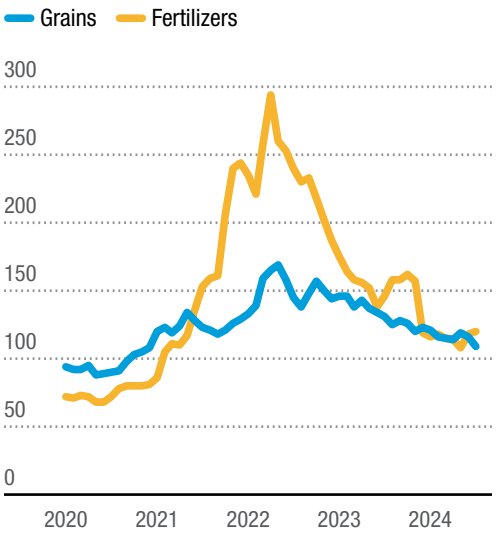
Unlike all other cereals, the price of rice has not fallen below its February 2022 level. After a slight decline in early 2023, the benchmark price of Thai rice surged by 35 per cent from March to December (figure II.12). This increase occurred due to export restrictions enacted by important exporters of rice (for example, India) to boost domestic supplies and food security in response to rising domestic prices and robust demand in Asia and Africa. The first quarter of 2024 saw a slight decrease in the benchmark price, driven by the depreciation of the currencies of major exporters against the United States dollar, sluggish global rice demand amid higher prices and an increase in seasonal supply.

Global maize production and exports are expected to increase slightly whereas opposite projections prevail for wheat.

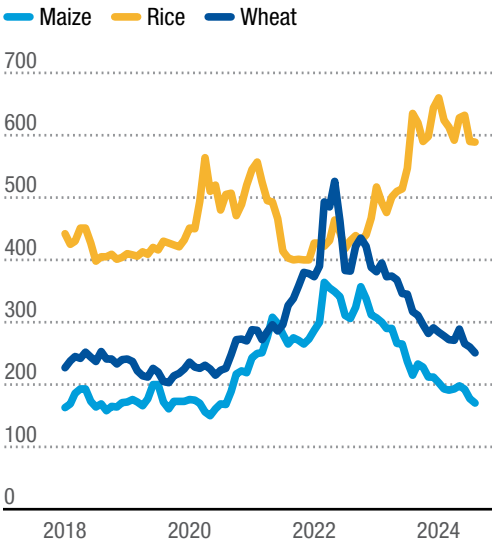
World rice production is forecast to rise, but not international rice exports, which may result in upward aggregate food price pressures. High food prices and inflation may also persist because of oligopolistic market structures. In the grains market, the top four companies control between 70 and 90 per cent of global trade (UNCTAD, 2023a), while markets for production inputs, such as fertilizers, seeds and technology, are also increasingly concentrated (see chapter III). To ensure market access for importing developing countries and alleviate their financial burden, it is essential to prevent anti-competitive trade practices.

Figure II.12
Food and fertilizer prices are declining except for rice

A. Grains and fertilizers
(2010=100)



B. Selected food commodity benchmark prices
(Dollars per metric ton)



Source: UNCTAD based on UNCTADstat and the Commodities Price Data (The Pink Sheet) of the World Bank.

Note: Data ends in July 2024.

D. Net capital flows to developing countries: The recovery is still fragile and uncertain

Net capital flows to developing countries returned to positive territories during the first quarter of 2024 after registering negative values over nine quarters in a row.[10] This means that, in aggregate, resident units from developing countries again became net borrowers vis-à-vis non-resident units from developed ones.

Region-wise, this favourable performance reflects, primarily, the increase in net inflows to Latin America and the Caribbean compared to the three last quarters of 2023, which were more than sufficient to compensate for net outflows from the other two developing regions. Net inflows to Latin America and the Caribbean have remained positive over the years, but since the pandemic have had a more volatile pattern and have not come back to the higher levels recorded over 2011–2014.

Another factor behind this improved situation was the gradual diminution of net outflows in developing Asian economies after their mid-2022 highs, mostly on the back of development in China, Hong Kong (China) and Singapore, although net outflows during the first quarter of 2024 were slightly larger than the ones of the last quarter of 2023. Africa recorded a small net outflow after a positive but subdued performance in 2023 (figure II.13).

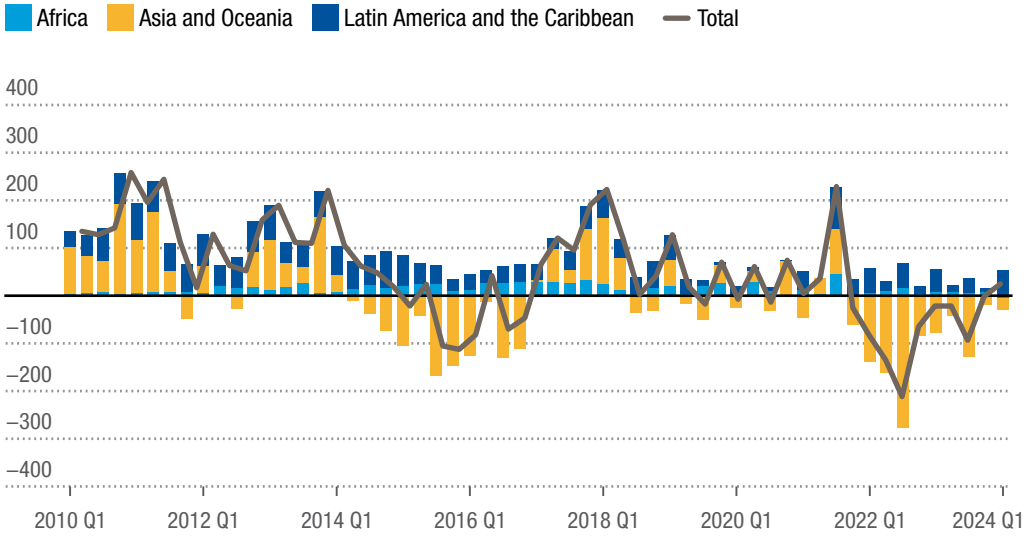
The last episode of persistent aggregate net outflows from developing countries occurred over 2014–2016. As in the recent episode, it was due to net capital outflows from developing Asia, more specifically, East Asia (table II.3). The main drivers of such outflows differed markedly between the two periods, however. The mid-2010s episode was centred around stock market turbulence in China, following the 2013 taper tantrum, with net outflows in other investments predominating.

[10] In this section, net capital flows refers to the sum of net direct investments, net portfolio investments and net other investments from the financial account of the balance of payments. It captures non-resident net flows minus resident net flows, excluding “derivatives” and “reserves and related assets”.

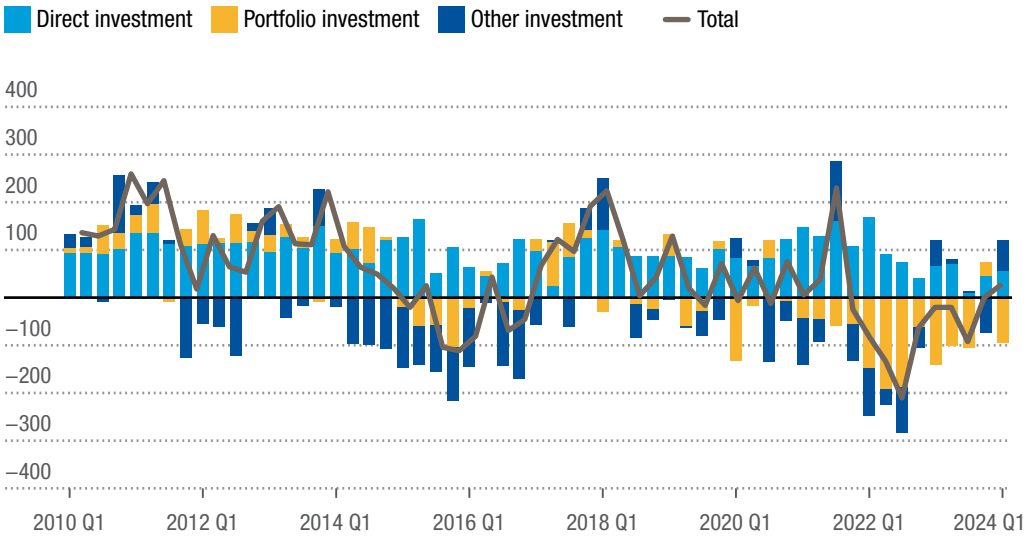
Figure II.13
After nine negative quarters, capital flows to developing countries rebounded in early 2024

Quarterly net capital flows to developing countries, selected regions and types
(Billions of dollars)

A. By region



B. By type



Source: UNCTAD based on the Balance of Payments database of the IMF.

Notes: Q1, first quarter. Net positive liabilities in the source data are valued as positive inflows and net positive assets as negative ones. Portfolio investment includes debt and equity. Other investment includes short and long-term bank lending. Total capital flows refer to the sum of direct, portfolio and other investments, i.e. the three classes of investments in the financial account of the balance of payments outside the direct and effective control of monetary authorities.

Table II.3
Net capital flows to developing countries

Yearly net capital flows to developing countries, selected regions and types
(Billions of dollars)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023[a]
▶ Developing countries	**617**	**490**	**279**	**566**	**185**	**-193**	**-150**	**483**	**400**	**208**	**128**	**280**	**-484**	**-116**
Direct investment	408	508	480	485	397	456	317	343	434	349	363	564	387	185
Portfolio investment	112	109	140	49	119	-255	-49	203	-37	-45	-128	-212	-594	-278
Other investment	97	-127	-341	32	-331	-394	-418	-63	3	-96	-107	-72	-276	-23
Of which:														
▶ Africa	**17**	**34**	**63**	**83**	**83**	**94**	**105**	**132**	**70**	**84**	**41**	**80**	**48**	**18**
Direct investment	46	36	48	39	63	49	40	46	30	36	18	72	39	13
Portfolio investment	6	8	27	23	8	25	17	47	3	32	0	-40	-30	-1
Other investment	-36	-10	-12	21	12	20	47	39	38	16	23	49	40	6
Of which:														
▶ North Africa	**11**	**-1**	**14**	**19**	**22**	**34**	**47**	**35**	**26**	**28**	**28**	**37**	**11**	**.**
Direct investment	10	5	8	11	11	11	12	12	13	13	9	9	14	.
Portfolio investment	8	-11	-3	1	1	2	2	23	-2	12	3	4	-23	.
Other investment	-7	5	9	7	10	20	33	0	15	2	17	25	20	.
▶ Sub-Saharan Africa	**6**	**35**	**49**	**64**	**61**	**60**	**58**	**97**	**44**	**56**	**13**	**43**	**38**	**18**
Direct investment	36	31	40	28	51	38	28	34	17	23	9	63	25	13
Portfolio investment	-1	19	29	22	7	23	15	24	5	19	-3	-43	-6	-1
Other investment	-29	-16	-21	14	2	0	14	39	23	14	7	24	20	6
▶ Asia	**385**	**196**	**-22**	**260**	**-153**	**-456**	**-386**	**208**	**142**	**26**	**52**	**43**	**-671**	**-233**
Direct investment	252	315	267	292	190	272	148	171	258	200	243	390	221	39
Portfolio investment	4	-6	28	-75	3	-331	-113	114	-58	-75	-132	-185	-555	-258
Other investment	128	-114	-316	43	-346	-398	-421	-77	-58	-99	-59	-162	-337	-1
Of which:														
▶ Central Asia	**-10**	**-8**	**-5**	**2**	**6**	**10**	**9**	**7**	**-1**	**6**	**19**	**9**	**-6**	**8**
Direct investment	6	11	13	10	6	6	16	6	6	9	7	5	11	5
Portfolio investment	9	-13	-17	-6	-1	6	-1	6	-3	-4	9	6	-13	-4
Other investment	-24	-6	0	-1	1	-1	-7	-4	-4	1	3	-1	-4	8
▶ East Asia	**277**	**256**	**-31**	**316**	**-69**	**-429**	**-438**	**112**	**142**	**-30**	**-53**	**-88**	**-304**	**-262**
Direct investment	176	238	170	215	135	171	14	52	118	78	127	212	38	-134
Portfolio investment	-33	16	43	-9	69	-204	-115	54	33	15	21	-35	-325	-111
Other investment	134	2	-243	111	-273	-396	-336	6	-9	-123	-201	-266	-17	
▶ South Asia	**82**	**66**	**93**	**70**	**82**	**86**	**37**	**102**	**84**	**107**	**85**	**147**	**66**	**75**
Direct investment	16	28	19	31	28	42	46	35	37	43	58	32	39	18
Portfolio investment	38	2	32	9	45	11	-4	34	-10	27	11	7	-19	31
Other investment	28	36	43	30	9	33	-5	33	57	37	16	108	46	27
▶ South-East Asia	**37**	**-5**	**3**	**-36**	**-50**	**-69**	**-23**	**25**	**15**	**-12**	**10**	**42**	**-172**	**-27**
Direct investment	42	32	50	46	37	56	59	82	97	83	55	126	147	150
Portfolio investment	8	11	-43	-59	-49	-74	-2	-4	-58	-97	-82	-86	-75	-109
Other investment	-12	-48	-4	-23	-39	-51	-80	-53	-24	3	37	2	-243	-68
▶ West Asia	**-1**	**-114**	**-82**	**-92**	**-122**	**-54**	**30**	**-38**	**-99**	**-46**	**-9**	**-66**	**-256**	**-27**
Direct investment	14	6	15	-9	-17	-3	14	-4	-1	-13	-4	14	-14	1
Portfolio investment	-16	-23	14	-9	-61	-70	9	24	-20	-16	-91	-76	-122	-65
Other investment	2	-97	-111	-74	-45	18	8	-59	-78	-17	86	-4	-119	37
▶ Latin America and the Caribbean	**212**	**258**	**234**	**218**	**256**	**171**	**132**	**146**	**191**	**102**	**36**	**161**	**138**	**99**
Direct investment	107	155	162	151	142	133	128	126	147	114	103	104	127	133
Portfolio investment	101	106	84	101	108	51	47	43	17	-2	5	13	-10	-18
Other investment	4	-3	-13	-34	7	-14	-43	-22	27	-10	-71	44	20	-16
▶ Oceania	**3**	**2**	**4**	**5**	**-1**	**-1**	**-1**	**-4**	**-3**	**-4**	**-1**	**-5**	**1**	**.**
Direct investment	2	2	3	3	2	2	1	0	0	0	-1	-1	0	.
Portfolio investment	0	1	1	0	0	0	0	0	0	0	0	0	0	.
Other investment	1	0	1	3	-4	-3	-2	-3	-4	-3	0	-3	1	.

Source: UNCTAD based on the Balance of Payments database of the IMF.

Notes: Net positive liabilities in the source data are valued as positive inflows and net positive assets as negative ones. Portfolio investment includes debt and equity. Other investment includes short and long-term bank lending. Total capital flows refer to the sum of direct, portfolio and other investments, i.e. the three classes of investments in the financial account of the balance of payments outside the direct and effective control of monetary authorities. Due to rounding, some totals may not correspond with the sum of the separate figures.

[a] Indicates preliminary estimates.

By contrast, because negative outflows between the fourth quarter of 2021 and the end of 2023 were associated with monetary tightening in developed countries and deteriorating global financial conditions (UNCTAD, 2023a), they were more broad-based geographically, with several countries in all developing regions experiencing a pattern similar to the one that the aggregate for developing countries depicts. This time, however, "portfolio investment" in general and the sale of domestic bonds by non-residents in particular played larger roles, followed by outflows in other investments. Foreign direct investment performance also deteriorated, especially in 2023 in Africa and developing Asia.

It is important to note that developments observed over the last two to three years suggest more profound structural shifts among international investors due to current geopolitical tensions. Complacency about the positive dynamics observed during the first quarter of 2024 is not warranted. Overall financial conditions remain fragile and volatile, particularly for developing countries.

Preliminary data for the second quarter of 2024, based on monthly portfolio flows for a handful of large developing countries with available information, points to the waning of momentum, casting doubts on the robustness of trends observed at the beginning of 2024. This echoes financial investors' realization that the easing of monetary policy in the United States, particularly, did not occur as swiftly as previously expected.

The unwinding of the yen carry trade in August 2024 acted as another signal of potential troubles ahead, even though the panic that hit financial markets at that time seems, so far, to have been short-lived and contained, with limited implications for the real economy. Nevertheless, the magnitude of the swings observed in several currency and stocks markets in early August left many agents rather insecure about the overall current financial environment. There is no doubt that the instability in today's financial markets is not creating favourable terrain for long-term key investments.

1. Direct investment: Geoeconomic fragmentation is reshaping the landscape

In the context of current discussions about the relocation of firms and more long-term structural changes, foreign direct investment data point to slowing flows amid recent global and regional crises. Flows remained subdued in 2023 for a second consecutive year. In absolute terms, foreign direct investment fell 7 per cent in the developing world to $867 billion, mainly due to an 8 per cent decrease in developing Asia, though flows retreated as well in Africa and Latin America and the Caribbean, by 3 per cent and 1 per cent, respectively.

More broadly, empirical evidence shows that geoeconomic fragmentation is reshaping the landscape of global direct investment as trade networks are fragmenting, regulatory environments are diverging, and international supply chains are being reconfigured (UNCTAD, 2024b; 2024j). All investment patterns are not changing in the same ways, however. Apple (United States), for instance, scaled down its operations in China to diversify its supply chain. By contrast, data for the first half of 2024 point to large German carmakers reinforcing their presence in Chinese manufacturing; they reinvested about half of profits earned there to expand production (Schmitz and Matthes, 2024). Part of the reason for this lies in global carmakers not wanting to lose their relative share of the world's largest and most dynamic market. Beyond such anecdotal evidence, however, the overall picture looks gloomy as high uncertainties hardly support long-term planning. They can lead to postponing or scaling down investment decisions in the short to medium term.

Net capital flows to developing countries returned to positive territory in 2024, yet vulnerabilities remain.

The direct investment picture for developing countries, in aggregate, does not support long-term planning.

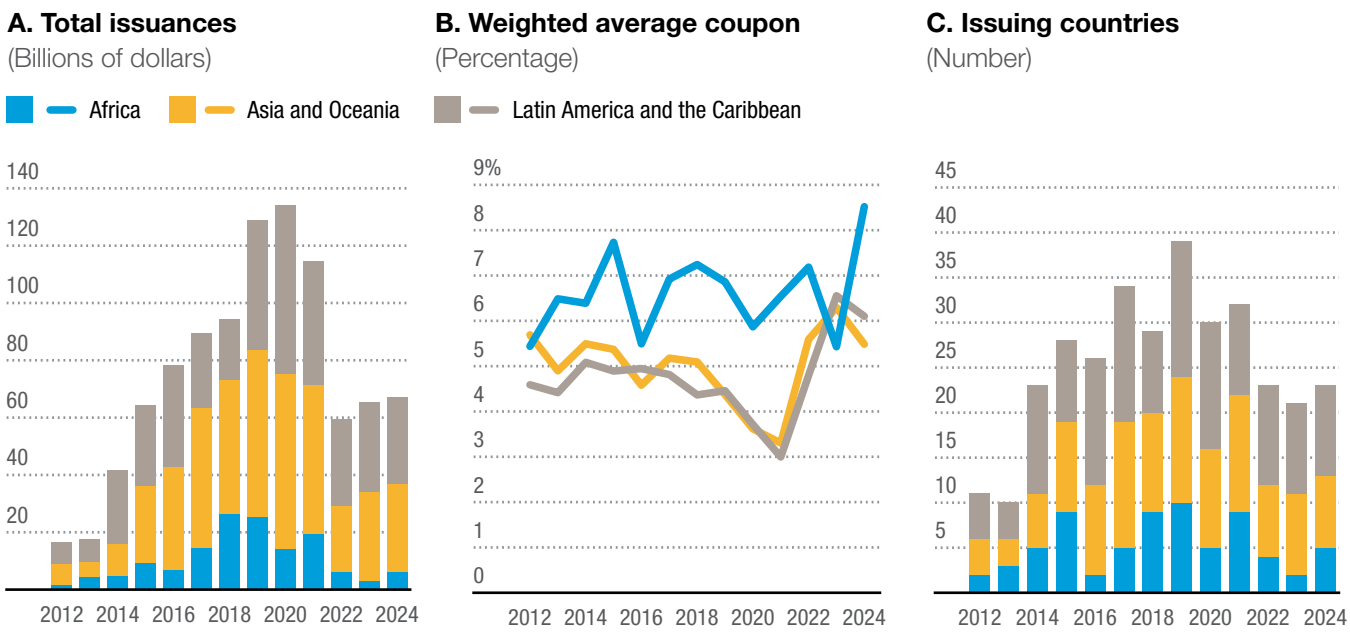
2. Portfolio investment: Financing conditions remain harsh for many developing countries

Available portfolio investment data for a handful of emerging market economies suggest that, after hitting a low point over the past two years, the momentum of non-resident capital flows to these economies changed direction in the first quarter of 2024. Some large emerging market economies returned to international bond markets, at times with record issuances (UNCTAD, 2024h). This shift is partly due to a slightly more favourable outlook for developing countries compared to advanced economies (chapter I). It also results from improved global financial conditions owing to expectations of interest rate cuts in the United States and Europe, even though financial investors, in aggregate, appeared at times too optimistic regarding the expected decline in interest rates.

A deeper look calls, however, for a more cautious and less rosy diagnostic for at least two types of arguments. The first relates to sovereign debt in developing countries. As seen in figure II.14, 2024 issuances of new debt between January and August exceeded levels recorded for the entire year in both 2022 and 2023, highlighting the revival of appetite by international investors for developing countries' public external debt. Yet aggregate flows remain below the 2019–2021 peak years and probably also below the three previous years. Moreover, the value of sovereign bond issuances in 2024 in Africa remains below levels observed since 2015.

The average coupon of 2024 issuances is higher than historical levels in all developing regions, which raises concerns about increasing debt servicing that diverts

Figure II.14
Borrowing costs are still high while new sovereign bond issuances are rebounding in developing regions
Total issuances, weighted average coupons and number of issuing countries of newly issued sovereign bonds, selected developing regions



Source: UNCTAD based on LSEG Eikon.

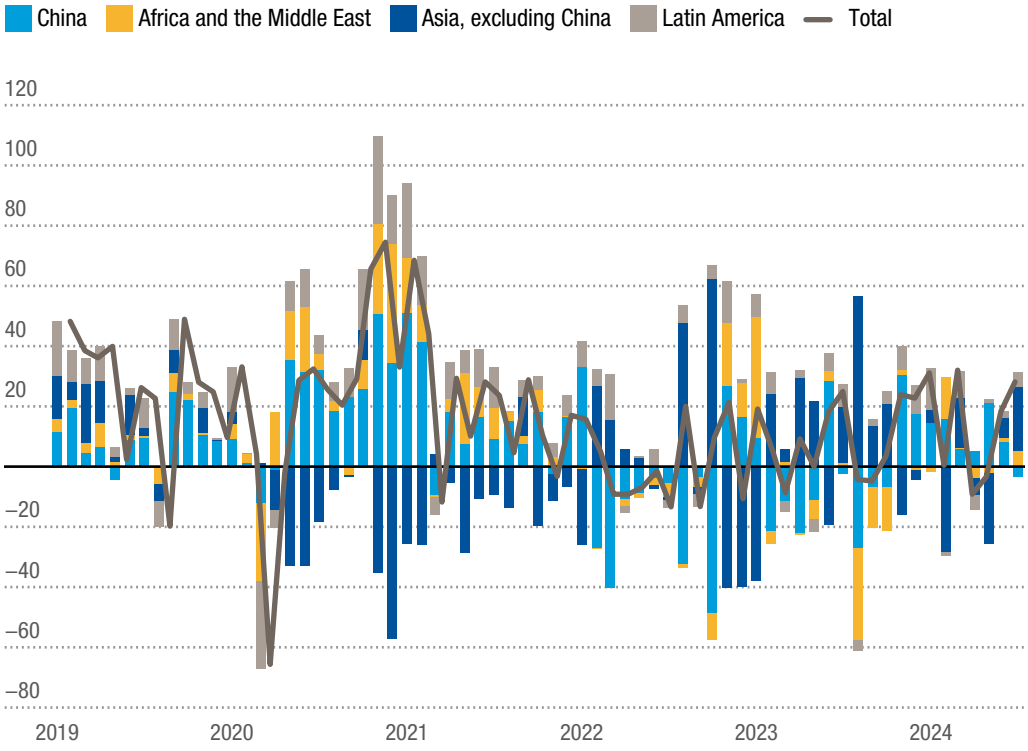
Note: Data relate to annual issuances of sovereign dollar, euro and yen bonds under foreign jurisdictions, excluding issuances in the context of debt restructuring. For 2024, data only comprise issuances until August.

essential resources away from development investments (figure II.14). Furthermore, the number of developing countries tapping the international bond market in 2024 has lagged behind what was typical in the years from 2015 to 2021 in general and is 40 per cent below a 2019 record. Overall, these patterns highlight how rising global interest rates since 2022 have further strained public budgets in developing countries. Interest payments are outpacing essential public expenditures such as health, education and climate action; one in three developing countries spends more on interest payments than on these critical areas for human development (United Nations Global Crisis Response Group-Technical Team, 2024).

Another argument relates to the plausible waning of momentum observed during the first quarters of 2024. Monthly portfolio flows for a sample of emerging market economies point to a significant slowdown of non-resident portfolio flows to developing countries during April and May 2024, except for portfolio investments in Chinese debt. Flows then bounced back, especially in July on the back of robust issuances in Mexico and Türkiye (figure II.15). Yet this volatility casts doubts on the robustness of trends observed at the beginning of 2024. It highlights how the waning of initial optimism in financial markets about the pace of monetary policy easing in the United States put upward pressure on global funding costs during the second quarter of 2024.

In August 2024, the Jackson Hole meeting brought positive news for developing

Figure II.15
Monthly portfolio flows suggest that momentum vanished after the first quarter of 2024
Non-resident portfolio flows to China and selected developing regions
(Billions of dollars)



Source: UNCTAD based on Institute of International Finance database.

Note: Data ends in July 2024. Developing economies considered in this figure comprise Brazil, Chile, China, Taiwan Province of China, Colombia, Ghana, India, Indonesia, Kenya, Lebanon, Malaysia, Mexico, Mongolia, Pakistan, the Philippines, Qatar, Saudi Arabia, South Africa, Sri Lanka, Thailand, Türkiye and Viet Nam.

countries, confirmed on 18 September when the Federal Reserve of the United States cut its policy rate by 50 basis points, more than two and a half years after it started hiking borrowing costs. The outlook remains clouded with uncertainties regarding the magnitude and timing of subsequent cuts, however. The forthcoming presidential election in the United States also brings unpredictability. Concerns about interest rate levels are particularly acute given heightened vulnerabilities linked to the public and publicly guaranteed debt of developing countries (box II.2) and the significant debt renewal that developing countries will face as they address their maturity wall in 2024 and 2025.

Box II.2
The sovereigns of frontier market economies are not out of the woods yet

An asymmetry exists between two groups of financially integrated developing economies: the emerging market economies and the frontier market economies. The former are mostly upper-middle-income countries that have integrated into international capital markets since the 1990s. The latter are mainly low- or lower-middle-income countries that began to tap this market after the global financial crisis of 2008.

Because frontier market economies issue mostly speculative-grade sovereign bonds with high-yield assets for global investors, they tend to have greater spread volatility and are the first to be sold during global financial shocks. Since many pension funds are precluded from investing in non-investment grade debt instruments, more speculative asset managers and investors (such as hedge funds) predominate in the ownership of such securities.

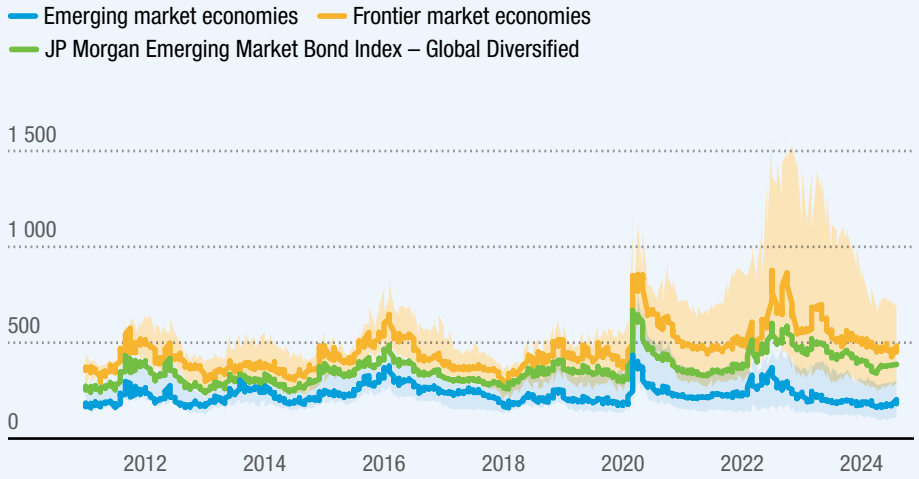
Consequently, the external sovereign bonds of frontier market economies faced sharper spread increases than those of emerging market economies from 2019 to mid-2023, when global financing conditions deteriorated. Sharper reversals also took place when global financial conditions improved between the last quarter of 2023 and the first quarter of 2024. As frontier market economy sovereign bond prices reached record lows, global investors again bought in, compressing their spreads closer to those of emerging market economies (UNCTAD, 2024g).

Frontier market economy sovereigns have therefore regained access to global capital markets, albeit at a higher cost given increased interest rates in major developed economies, particularly the United States. Further, spreads of emerging market and frontier market economies with respect to the United States benchmark have only returned close to the average level between the global financial crisis and the start of the COVID-19 pandemic. Key benchmark rates used to be much lower.

In this context, it is not surprising that the external and public sector debt sustainability of two thirds of developing countries worsened between 2017 and 2023, with frontier market economies registering sharper deterioration. External debt servicing costs have risen more quickly than foreign exchange earnings and interest cost growth has outstripped that of government revenues (United Nations Global Crisis Response Group-Technical Team, 2024). In 2023, public and publicly guaranteed debt in frontier market economies reached an estimated $684 billion, a threefold increase since 2010. This compared to 2.4 times for emerging market economies and 1.8 times for other developing economies that have limited integration into global capital markets and rely mainly on external public financing and official development assistance.

Yields of sovereign bonds in frontier market economies have not receded to pre-COVID-19 levels

Weekly spreads with respect to Treasury bonds of the United States, selected economies, July 2011–August 2024
(Basis points)



Source: UNCTAD based on country-level data from the JP Morgan Emerging Market Bond Index.

Note: The bold lines for the emerging market and the frontier market groups of economies correspond to the median of each group, computed from economy-specific data available in JP Morgan's Emerging Market Bond Index – Global Diversified. The shaded areas refer to the interquartile range.

The total external debt servicing costs of frontier market economies increased by about 550 per cent from 2010 to 2023 (an average of 15.5 per cent a year), compared with 174 per cent (8.1 per cent per year) and 121 per cent (6.3 per cent a year) for other developing economies and emerging market economies, respectively.

The frontier market economy sovereign external debt build-up has primarily been accompanied by increasing sovereign debt servicing that shrinks resources for crucial public expenditures. Debt servicing on public and publicly guaranteed debt relative to government revenues surged from almost 6 to 15 per cent between 2010 and 2023. This contrasts with the figure for emerging market economies of around 3 per cent, and for other developing economies of just over 7 per cent in 2023, half the figure for frontier market economies.[a]

These patterns raise concerns about the ongoing sustainability of both external and public debt for developing countries, and the extent to which the servicing of such debt drains resources from development in the context of the vast financing gap for achieving the goals of the 2030 Agenda and the Paris Agreement.

Source: UNCTAD (2023a, 2024g); United Nations Global Crisis Response Group-Technical Team (2024).

[a] Group averages conceal differences across economies. Considering the top 25 developing economies with the highest ratios of public and publicly guaranteed debt servicing to government revenues in 2023, 2 were emerging market economies, 10 were frontier market economies and 13 were other developing economies. Sovereigns from the last group also confront high debt vulnerabilities, particularly those with lower-middle- and low-income levels. Among these 13 countries, only 2 are upper-middle-income (Belize and Mauritius).

3. Other investment, including interbank lending, diverges across developing regions

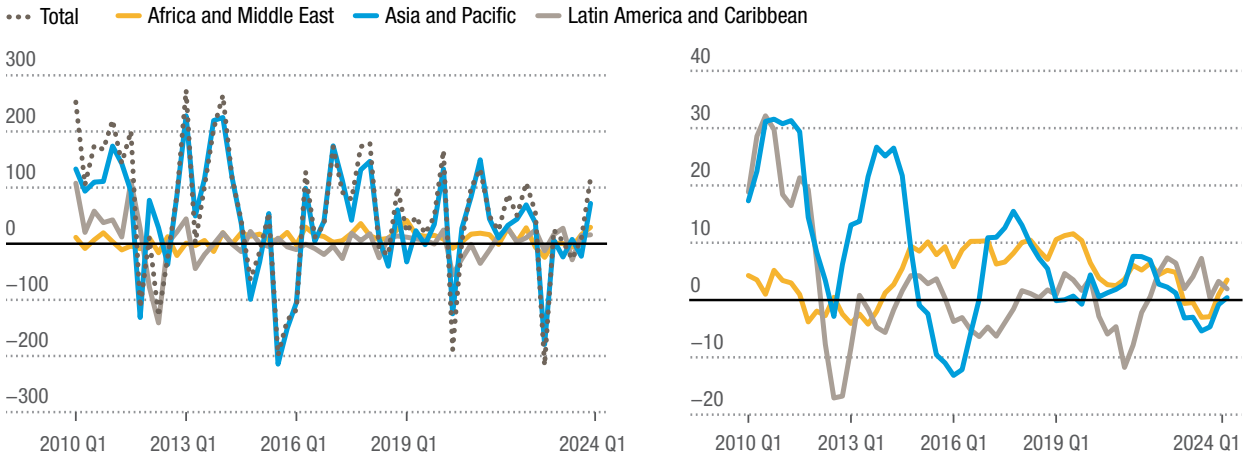
Net other investment flows to developing countries have oscillated between positive and negative territories in recent quarters, reflecting their volatile nature. Cross-border bank lending, one of its components, experienced similar patterns. Bank for International Settlements (BIS) locational banking statistics show that banks' global cross-border claims to residents of developing countries in Africa and the Middle East, Asia and the Pacific, and Latin America and the Caribbean rose sharply by $117 billion over the first quarter of 2024 on a foreign exchange and break-adjusted basis, following a meagre increase during the last quarter of 2023. Of these claims, credits – which comprise loans and holdings of debt securities – accounted for almost $100 billion (figure II.16). These flows comprised the largest quarterly increase of the past three years, on the back of record high lending of $49 billion in Chinese renminbi, reflecting the growing value of cross-border credits by banks in Chinese currency (*Financial Times*, 2024b).

Credit expansion diverged somewhat across regions. Credit to Asia and the Pacific expanded by $64 billion, restoring annual growth to positive territory (0.4 per cent). Credit to residents in Africa and the Middle East expanded by $29 billion with year-on-year growth reaching 3.5 per cent. Credit to entities in Latin America and the Caribbean grew by $6 billion, driven by robust credit to borrowers in Brazil, which expanded by 8 per cent annually (figure II.16), although year-on-year growth for the region overall decelerated to 2.0 per cent. Dollar-denominated foreign currency credit to non-banks in developing countries grew about 1 per cent, the first positive figure in nearly two years (BIS, 2024).

Figure II.16
International bank lending to developing countries rebounded during the first quarter of 2024

A. Banks' global cross-border claims to residents of selected developing regions
(Billions of dollars on a foreign exchange and break-adjusted basis)

B. Year-on-year changes in cross-border bank credit to selected developing groups
(Percentage)



Source: UNCTAD based on the Locational Banking Statistics database of the BIS.

Notes: Q1, first quarter. Claims refers to "all instruments" on bank balance sheets, comprising credits (loans and deposits as well as holdings of debt securities) and residual other instruments. Annual changes are adjusted according to BIS (2019). Country group classification relies on BIS criteria.

4. On the way to the fourth International Conference on Financing for Development

As preparations gear up for the 2025 fourth International Conference on Financing for Development, the recent evolution of cross-border capital flows indicates that external private finance has fallen short of what is needed to bridge the large and growing gap in financing to achieve sustainable development (United Nations, 2024).

According to UNCTAD estimates, as of 2023, the annual investment gap for the Sustainable Development Goals had increased to $4 trillion, about 60 per cent more than the $2.5 trillion estimated on the adoption of the 2030 Agenda (UNCTAD, 2023b). This additional gap stems from two critical trends. The first is underinvestment. The pace in the growth of investments in the Sustainable Development Goals was below 2014 ambitions, with the COVID-19 pandemic playing a key role in slowing progress. Moreover, higher interest rates have exacerbated weak investment trends in the private sector. Elevated costs of capital have been particularly harmful for investments in capital-intensive renewable energy because they are relatively sensitive to monetary and financial conditions (United Nations, 2024). The second trend entails additional needs associated with cascading crises and mounting estimates of the investment needs for climate change mitigation and adaptation.

While net capital flows returned to a positive level in developing countries in the first quarter of 2024, it is uncertain if this trend will continue. The procyclicality and high volatility of capital flows, particularly portfolio investment and cross-border bank lending, mean that external private financing disappears when it is most needed. This tendency is compounded by disappointing trajectories in foreign direct investment linked to geoeconomic fragmentation.

Several takeaways could be kept in mind as United Nations Member States prepare for the 2025 conference. First, hopes that blended finance would help to mobilize private financing resources have not been realized; the “billions-to-trillions” mantra has never delivered on its promises. Second, addressing sovereign debt vulnerabilities in developing countries requires policy action to stop a growing development crisis (box II.3).

Private finance is falling short of what is needed to bridge the sustainable development financing gap.

Box II.3
Dealing with sovereign debt vulnerabilities in developing countries

Cascading crises – the pandemic, the war in Ukraine, a deepening climate crisis, a cost-of-living crisis and escalating geopolitical tensions and conflicts – and the most aggressive monetary tightening in developed countries since the 1970s have intensified an already unsustainable sovereign debt position for many developing countries (box II.2).

While a systemic external debt crisis – where a growing number of countries move simultaneously from distress to default – has not taken place, a development crisis is under way, with rising external and public debt servicing draining resources from the 2030 Agenda and Paris Agreement ambitions.

Current debt challenges and the consequent development crisis are deeply rooted in the inequities of the hierarchical international monetary and financial system, which has become increasingly disconnected from development priorities, as evidenced by the latest trends in external private financing.

Against this backdrop, for countries experiencing deteriorating external debt sustainability, there are two broad sets of policy responses that do not include efforts to curtail economic growth. The first set comprises measures aimed at reducing external debt by decreasing the need for imports and/or expanding and diversifying exports over time. The second set entails reducing the average cost of servicing external debt. The former relates primarily to trade and industrial policies that bring about structural changes in the import and export propensities of the economy. The latter broadly relates to the ability of countries to access private and official capital flows, and the terms governing how they do so (UNCTAD, 2024d). The experience of frontier market economies (box II.2) reveals that access to private capital flows may expand capital available but at a high price – especially if it substitutes for concessional finance from official sources due to a graduation in income level.

In this context, as detailed by UNCTAD (2023a), changes to the prevailing global financial architecture along the five stages of the debt life cycle could reduce the costs of development financing. For private external capital to developing sovereigns, the following transformational proposals could be considered:

1. **Revisiting the UNCTAD Principles on Promoting Responsible Sovereign Lending and Borrowing** to align them with broader development financing needs, innovative financial instruments and the new creditor landscape
2. **Creating an international loans repository** to improve debt management by digitizing loan transactions, ensuring consistent financial terms and providing reliable statistics
3. **Establishing a multilateral sovereign debt workout mechanism** with ensured participation of all creditors, including private lenders, on comparable terms
4. **Setting up a borrower's club to discuss technical issues and innovation** as well as sharing experience and advice
5. **Initiating an automatic standstill for countries declaring distress**, to concentrate the minds of creditors in the workout process
6. **Defining international and domestic rules** for a standstill on debtors' obligations during climate, health and other external crises.

Source: UNCTAD (2023a, 2024d).
Note: These six bullet points are a subset of UNCTAD proposals to address sovereign debt vulnerabilities in developing countries.

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Chapter III

Globalization at an inflection point

In a major challenge for developing countries, current global economic and geopolitical shifts in globalization could limit export-led growth strategies. Changing technology and market structure, 'deglobalization' and worsening security environment endanger development strategies based on expanded manufactured exports and some resource exports.

The complex effects of new technologies, including through a higher concentration of corporate control, may be mostly negative for commodity exporters, although lower-cost electrical power will bring benefits. Dependence on critical and scarce materials for batteries exacerbates these risks, as their supply chains are prone to disruptions and hence price volatility and shortages.

In addition to being labour-replacing, as in the past, new technologies are concentrated in a handful of companies. Some technologies favour homeshoring, making governance issues and international policy coordination increasingly important.

The technological characteristics of the emergent sixth wave of economic growth – biotechnology, artificial intelligence and renewable energy – do not offer a well-defined guide for development strategies. Much will depend on the management of stresses on trade and finance. Services-export-led growth as a path to development will only remain feasible if new policy barriers are not enacted and access to markets and technologies is safeguarded.

A delayed or absent political response to the sway of new technologies, including artificial intelligence, will likely leave a vast and critical area of the global economy controlled by large corporations and private regulatory bodies. This will be neither inclusive nor in the public interest.

United Nations

Key policy takeaways

- **A wide implementation of sixth-wave technologies and energy transition threaten** to reduce major export revenue sources for developing countries. Reducing current debt burdens is thus vital for enabling their financial sustainability in the changing global economy.
- **WTO rules on industrial subsidies and trade barriers need to be reconfigured** to enable market access and fair competition, and to support raw materials exporters to expand the value added of their exports.
- **Coordinated policy mechanisms** to stabilize domestic agricultural production and prices can help relieve current financial and debt service stress in the global South.
- **The advanced world should live up to its existing climate change promises** to help fund the energy transition in developing economies.
- **Artificial intelligence needs to be globally governed by agreed principles and standards** to avoid regulatory fragmentation. These efforts should be paralleled by greater policy coordination to limit the concentration of corporate power, enhance transparency and enable competition.

A. Introduction

Eighty years since the Bretton Woods Conference, the world trade regime and the global economy more generally appear to have arrived at an inflection point. Seemingly settled assumptions, norms and institutional arrangements around trade, development, technology and security are all under question.

The inflection point is geoeconomic and geopolitical in nature, an outcome of the interplay of four ongoing shifts setting long-term conditions for development and growth:

- First, trade liberalization measures typical of the decades after 1990 are shifting towards more fundamentally protectionist and interventionist policies.
- Second, immigration and international labour flow policies, which were historically much less open than trade and financial market policies, are becoming even more restrictive.
- Third, a host of conflicts has disrupted a relatively stable global security regime.
- Fourth, new technologies have the potential to fundamentally transform the global division of labour.

Each of these four shifts could limit possibilities to pursue export-led growth and development strategies. This poses a major challenge for developing countries,[11] where development plans almost always involve export-led growth.

The current inflection point in globalization accentuates many risks long faced by developing countries in global finance and debt architecture. At the same time, it opens opportunities for the global South to rearticulate needs and priorities at the multilateral level, as shown by the ongoing process to develop a United Nations framework convention on international taxation, initiated by the African Group at the United Nations.

An inflection point is nothing new; UNCTAD emerged during a similar era of rapid change 60 years ago. The decade after it was created in 1964 saw the culmination of the great wave of decolonization, the breakdown of the Bretton Woods system of fixed exchange rates and controls over international capital flows, the beginning and then failure to shape a New International Economic Order, and the dawn of the information and communications technology (ICT) revolution. Each decisively reshaped the range of development trajectories available to what was then inaccurately called the "Third World", but which more accurately also encompassed late developers in

[11] Here and throughout this chapter, emerging market and developing economies refer to countries aggregated under that label in the IMF World Economic Outlook report, available a https://www.imf.org/en/Publications/WEO/weo-database/2024/April/groups-and-aggregates. These countries are particularly reliant on trade, and within that, primary product exports to finance both growth and physical capital investment. They are thus the appropriate group for analysing the long-term effects studied in this chapter. This definition includes Albania, Belarus, Bosnia and Herzegovina, Bulgaria, China, Hungary, Montenegro, North Macedonia, Poland, Republic of Moldova, Romania, Russian Federation, Serbia and Ukraine among the emerging market and developing economies, while excluding the Republic of Korea; Singapore; Hong Kong, China; Macao, China; and Taiwan Province of China, which are defined as advanced economies.

both the "First" and "Second Worlds".[12] The 1960s and 1970s saw largely State-driven, often foreign debt-financed development projects intended to create domestic capital goods capacity by supporting mass production industry.

The world's population is experiencing a slow-moving demographic transition impelled by falling birth rates. This is likely to decrease the pool of working-age people over the next three decades and increase the number of older workers aged 55 to 64 years. According to the International Labour Organization (ILO), older workers could become a quarter of the global labour force by 2030 (Harasty and Ostermeier, 2020). Without immigration, some advanced countries are already experiencing shrinking, ageing populations that may consume fewer imported manufactured goods in the long run (e.g. McKinsey Global Institute, 2024). Slower population growth in many developing countries might tip them into a middle-income trap where domestic markets are still nascent even as advanced economy markets begin to shrink.

What do current inflection points mean for core UNCTAD trade and development concerns? Answering this question requires reflecting on the past policy record and applying conceptual tools to help anticipate the likely (yet not predefined) impacts of ongoing geoeconomic and geopolitical changes on growth and development strategies.

This chapter is organized into three sections. In section B, the general dilemma that developing countries face in catching up on trade and development is discussed. The objective is to show why trade and exports, even more so, matter, or, as Joan Robinson (1962: 45) said, why "the misery of being exploited by capitalists is nothing compared to the misery of not being exploited at all". Trade raises the question of "trade in what", and in section C, Joseph Schumpeter's (1939, 1942) argument about recurrent economic growth waves or creative destruction is used to understand the potential effects of new technologies on production and trade.

While growth waves and structural transformation have been central to development thought (Kaiser, 1979; Kondratieff and Stolper, 1935; Bairoch and Kozul-Wright, 1996), the Schumpeterian framework helps to capture the specifics of new economic sectors as well as technological and financial processes driving such transformations today.

Finally, the quality and direction of trade require answering the question of trade *with* and *by* whom. Section D examines the drivers and likely consequences of the inflection point in international trade. The analysis applies the framework presented in sections B and C to the question of prospective development paths and policy space given three major potential changes. Of these, the decline in the current open trade regime looms largest as a barrier to an export-led development strategy.

Where appropriate, the chapter considers how changes in broader security and financial regimes might affect potential development pathways; both themes are addressed in greater detail in chapters IV and V.

[12] These labels referred to political alignments. The First World denoted largely rich Western democracies and Japan. The Second World was the Communist bloc. The Third World comprised the non-aligned nations but by metonymy also developing economies.

B. Development arrives at a juncture

A few years before the first UNCTAD conference in 1964, the Estonian economist Ragnar Nurske (1952: 571) sought to capture the combination of self-reinforcing mechanisms hindering development by saying: "Poor countries are poor because they are poor."

Poor countries are poor because they lack investment capital and skilled labour, or more precisely, the human capital needed to operate the latest tools. What Trinidadian economist W. Arthur Lewis (1954) called "unlimited supplies of labour" depresses local wages. It inhibits investment in human and physical capital goods to propel the structural transformation of an economy from labour-intensive agriculture to manufacturing and higher-value services. Poor countries are also poor in physical capital, including, critically, transport and energy infrastructure as well as the financial market depth and stability needed for the massive investments required to move closer to the technology and development frontier. More subtly, poor countries lack the legal and bureaucratic capacity to regulate increasingly complex markets for both goods and finance.

Towering over all these factors is one critical issue: poor countries remain poor because they lack enough aggregate demand to induce anyone to invest to remedy the other deficits. As Thirlwall (2012) argued, insufficient local aggregate demand makes the additional aggregate demand generated by exports crucial for inducing sustained investment and absorbing any investment-disincentivizing oversupply of local labour. Lewis' two-sector model assumed, or at least hoped, that an expanding modern sector would eventually absorb the oversupply of labour in the traditional or backward sector, triggering rising wages. In turn, rising wages would induce firms to invest in human and physical capital. The "Lewis turning point" can be observed in, for example, China, from roughly 2004 to 2006 (Garnaut and Song, 2006), and in other East-Asian economies characterized by rapidly growing export volumes. It is rare without export growth (Schwartz, 1994; 2007).

Many industries in modern economies have minimum economies of scale[13] that exceed the capacity of the local market, as the automobile industry shows (box III.1). Even though economies of scale are substantially lower for many other manufactured goods, the most complex goods and many key generic inputs for manufactured goods still require high levels of throughput to attain levels consistent with profitability and long-term economic resilience. For instance, there is only room for two, perhaps three, large civilian aircraft manufacturers for the entire world (e.g. Truxal, 2024). From the standpoint of domestic and foreign investors, scale logics mean that it makes more sense to supply developing country needs with imports rather than domestic production, although large economies, such as Brazil, China and India, are obvious exceptions.

[13] A minimum economy of scale refers to the price point at which enough units can be sold to be profitable given a fixed capital investment.

Box III.1
The changing geography of car production reflects shifts in trade and investment

The evolution of global car manufacturing is often seen as a representative case of the international division of labour and global economic geography, and a major marker for evolving trade integration throughout the twentieth century. Automobile assembly has typically captured 80 per cent of maximum economies of scale with an annual production run of 50,000 vehicles built on the same platform, and maximum economies of scale with a production run of 250,000 vehicles. Internal combustion engine design and assembly has had an even higher threshold, at 400,000 units. The domestic markets of most developing countries – and indeed, many developed economies – cannot absorb anywhere near those volumes.

Domestic demand for vehicles in Australia or Brazil in the 1950s, for example, rarely exceeded 200,000 units of inevitably diverse vehicles (Jenkins, 1987). By 2023, Australia – the fourteenth largest economy in the world – absorbed 1.2 million light vehicles, and Brazil – the ninth largest – 2.2 million.[a] By 2023, profitable economies of scale required annual sales of 1 million vehicles using a given platform and 300,000 units for engines (Doner et al., 2021).

This is a very long reach not only for countries below the median national economy in terms of GDP, which in 2023 included Honduras, Senegal and Zimbabwe, depending on how GDP was measured, but also for those further up the list. Roughly 12,500 new cars of all types were sold in Cyprus in 2023, for example. Among wealthier economies, Austria and Israel buy about 250,000 to 300,000 new light vehicles annually. Poorer but more populous Thailand consumes about 850,000, mostly light commercial vehicles. Israel has no light vehicle production; Austrian car production is essentially one subcontractor to Volkswagen whose output is equivalent to a third of Austrian consumption. Thailand is a major vehicle exporter by virtue of being a platform for Japanese multinational enterprises.

The shifting geographic location of automobile production reflects changing patterns of global trade and investment. Even as vehicle firms began moving or subcontracting component production to lower-cost locations, such as in Mexico and Taiwan Province of China, and then eventually to Eastern Europe and China, they also began transitioning the assembly of cheaper, smaller cars to select developing economies. These had domestic markets that justified something close to an entire production complex and a location favourable for exports to a larger region. Examples included Mexico, the Republic of Korea and Spain in the 1980s, then Czechia, Slovakia and Thailand in the 1990s, and eventually Brazil, Indonesia and Morocco in the 2000s. In each case, the final product simply tended to be lower-value vehicles, such as the Romanian-built Dacia Logan, or lower-cost versions of more expensive vehicles sharing the same platform, such as Škoda's Octavia in relation to the Volkswagen Golf or Audi A3.

Box III.1 The changing geography of car production reflects shifts in trade and investment

This trend has continued for electric vehicles, where the same minimum and maximum economies of scale for assembly remain relevant. Even though batteries have replaced internal combustion engines, the scale economies for battery production appear similar to those for internal combustion engines at about 400,000 to 500,000 per factory. The shift to electric light vehicles will therefore not dramatically alter the logic of production, although the location might change at the margins.

Chinese firms currently dominate the world market for electric vehicles, following a strategic decision by the State to develop this industry. Today, China leads on production, manufacturing 58 per cent of all electric vehicles in 2023, and consumption, with 6.8 million cars sold in 2024 (IEA, 2024b). This is consistent with the current shift in global manufacturing from the 2010s to the present, marked by the emergence of a larger consumer market in China. There is heavy demand for electric vehicles in Europe and Northern America, with 4.6 million units sold in 2023 (IEA, 2024b), following the trend set in non-electric vehicles.

Nonetheless, the weight of batteries (which increase transport costs) and the logic of "produce where you sell" mean that most traditional automobile production zones will persist, albeit perhaps under different ownership. The ongoing displacement of Japanese-owned internal combustion engine vehicle production by Chinese-owned electric vehicle production in Thailand provides an example.

Sources: Doner et al. (2021); IEA (2024b); Klier and Rubenstein (2022); Yang (2023).

a Data from the International Organization of Motor Vehicle Manufacturers available at https://www.oica.net/production-statistics/.

Importing almost all manufactured goods, however, has proven to be a recipe for persistent relative and perhaps absolute poverty, as Prébisch (1950) argued. Raw materials exports have combined the worst of two worlds: secularly declining prices as Ernst Engel's (1895) law took hold combined with extreme cyclical volatility for both prices and export quantities. Engel's law underlay the declining terms of trade that Prébisch observed. As income rises, the proportion spent directly on food, fibres and other raw materials diminishes (box III.2).

Box III.2
Engel's law suggests the risks from relying on exports of raw materials

Ernst Engel, a Prussian statistician, observed in 1857 that, as household income rose, the percentage of income spent on food declined even if absolute expenditure on food increased. Although Engel did not directly address raw materials more generally, his analysis has important implications for the raw materials intensity of consumption and thus for the ability of developing countries to export raw materials.

Put simply, the rate of growth in a given developing economy is limited by the rate of growth of exports, as Thirlwall (2012) argues more generally. But here, specifically, if raw material exports and demand for them grows more slowly in an economy than overall global demand, income growth in that economy will lag the world in general. In short, the economy will lose ground relatively if not absolutely. This relative decline was Prébisch's (1950) core concern.

Box III.2 Engel's law suggests the risks from relying on exports of raw materials

A counterargument might be that absolute consumption of raw materials always increases. For example, past technological revolutions consistently involved shifts in the main source of energy (see the special focus section). Coal seemingly replaced waterpower or wood; petroleum seemingly replaced coal. But this displacement is more apparent than real, because in each case, the older source of inorganic energy continued to be important in terms of absolute volumes, even as its percentage share of total energy output declined. Global coal output and consumption grew even as oil and natural gas became dominant in transport and electricity generation.

The highest-ever level of coal production was in 2023, at 179 exajoules (Energy Institute, 2024). Globally, coal demand has spiked 75 per cent since the 1997 Kyoto Protocol and nearly 15 per cent since the 2015 Paris Agreement on climate change. Just five countries consumed nearly 80 per cent of the world's coal in 2023: China, India, Indonesia, Japan and the United States (Blas, 2024). In 2024, global consumption of coal is projected to rise to another all-time high. Under current trends, consumption will be greater in 2050 than in 2000 (Blas, 2024). Some oil companies apply this historical pattern in predicting a continued expansion of oil consumption.

Historically, population growth drove continued absolute increases in raw materials consumption. Given a global demographic shift towards slowing or even reversing population growth, an absolute decline in coal consumption (and by extension, other raw materials) cannot be ruled out. On a per capita basis, coal consumption (mostly indirectly through electricity, steel and cement consumption) has been essentially stagnant for the past 40 years. Much of the overall rise in consumption is due to the once-only urbanization of China; it today accounts for 56 per cent of coal consumption globally (Energy Institute, 2024; Blas, 2024).

A second historical pattern has been rising incomes driving increasing raw materials consumption. But consistent with Engel's observations, higher incomes among the poor largely account for increased absolute consumption. This chapter's main contention is that low- and middle-income countries potentially face growing headwinds in raising incomes, particularly if they rely on raw materials exports.

Low- and middle-income countries risk headwinds in raising incomes, particularly if they rely on raw materials exports.

This imposes a constraint on development because the elasticity of demand in advanced countries for developing country exports limits the rate of growth of those exports. This, in turn, presents a barrier to growth, in so far as development involves imports of capital goods paid for by those exports (Thirlwall, 2012). In the context of slow population growth in developed economies, generating, for instance, novel food exports would not necessarily increase income for the aggregate of developing countries. Simultaneously, price and quantity volatility have made debt servicing difficult and hindered investment (UNCTAD, 2023c).

From a policy perspective, the intersection of Engel's law and self-reinforcing disincentives to productive investment suggest only one way out: export manufactured goods and use the export market to attain a profitable scale. Manufactures exports might not face the same saturation effects that agricultural exports confront, enabling the expansion of imports of capital goods needed to stand up industrial production. And manufactures exports usually generate productivity and knowledge spillovers – Verdoorn effects – through learning by doing and the need to meet global quality standards.[14]

[14] The economist P. J. Verdoorn (1980) estimated that a 1 per cent increase in output generated a 0.5 per cent increase in productivity and a 0.5 per cent increase in employment in a wide range of industries.

These spillovers are essential for absorbing labour in industries linked to firms that export, and for the upgrading that induces upstream investment in training and education. Manufacture exports can thus be engines of economic and human development. The current stagnation of global trade, however, endangers potential gains from learning by doing, scale economies and employment spillovers into the service sector. Rodrik (2013) argues that this premature deindustrialization is a significant driver of the "middle-income trap".

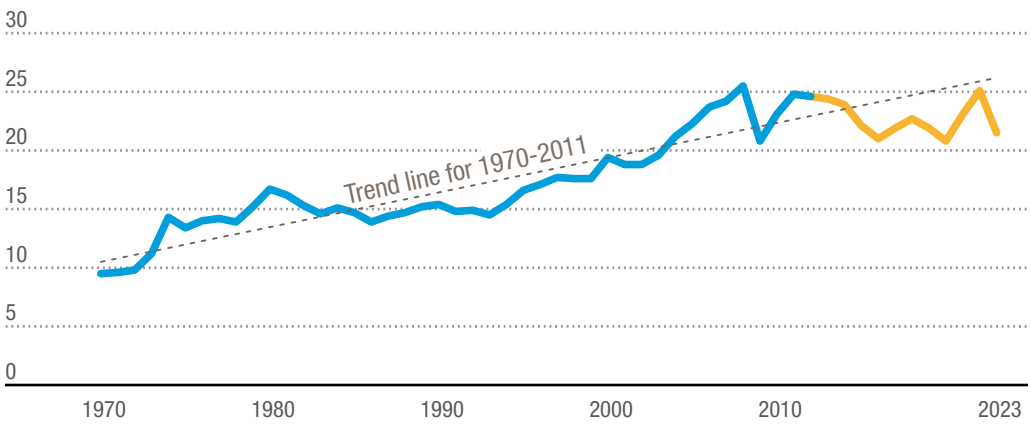
If industrial exports were possible, what forms would they take? In the decades after World War II, decolonization removed externally imposed barriers to industrial exports. And the gradual reduction of trade barriers for manufactured goods under the General Agreement on Tariffs and Trade from the 1950s onwards enabled exports from newly independent developing countries. A wave of outsourcing and offshoring ensued, shifting the manufacturing of many labour-intensive products to developing economies.

Yet today, manufactured goods exports might face some of the same problems as raw materials exports, compounded by the nature of the current inflection point. To explore why, a special focus section presents Schumpeter's arguments about growth waves and how they relate to the more general and abstract process of structural transformation.

In the current ICT, or fifth growth wave, many developing countries have added manufactured goods exports to their traditional resource portfolio. Some were forced to do so because they simply lacked exportable natural resources. But the majority did so by choice, as shown by the rapid growth in the number of export processing zones after 1965.

Transnational firms and giant retailers organized most of those trade flows. By 2012, internal (administered) trade by multinational enterprises accounted for one third of global trade by value. Purchases from firms they indirectly controlled accounted for another sixth, and arm's length purchases brought the total to two thirds (UNCTAD, 2013: 163). At that point, as figure III.1 shows, global trade levelled off as a share of global GDP, with absolute declines in current dollar terms in 2016, 2019–2020 and 2023.

Figure III.1
The fifth growth wave saw rapidly rising exports, but world trade has been levelling off
World trade as a share of global GDP
(Percentage)



Source: UNCTAD based on UNCTADstat database.

Growth waves shape the potential of exports for development

Joseph Schumpeter (1939, 1942) and Perez (2002) argued that the focus on equilibrium and competitive markets in textbook economics bore little relation to the reality of capitalist economies. Instead, as Joan Robinson (1962) and Nicholas Kaldor (1996) also argued, the economy was never in equilibrium. It was often characterized by high levels of oligopoly if not outright monopoly. Periods of relatively rapid growth and massive upheaval tended to be followed by eras of relative stagnation, the involution of new technologies, and the exhaustion of abundant social and material resources that fuelled the initial expansion. Schumpeter argued that six big changes characterized periods of rapid growth:

1. A new source of cheap energy, as with coal in the mid- to late-nineteenth century and then oil in the mid-twentieth century
2. A new production process based on a new general-purpose technology, as with continuous flow and then continuous flow assembly line production using electrically powered equipment
3. New investment or mass consumption goods, as with steel and then standardized consumer durables
4. A new mode of transportation, as with steel steamships and bicycles, and then automobiles and aircraft
5. A new form of corporate organization, as with the proliferation of vertically integrated firms with ownership divorced from management, and then Alfred Chandler's (1962) "M-form" multidivisional firm; related to that, new modes of financing investment
6. Less salient in Schumpeter but nonetheless very important: new modes of social and economic governance to balance supply and demand, as with early twentieth century cartels and then Keynesian welfare States (Boyer, 1990; Perez, 2002; Freeman, 2007).

Combined, these six changes manifest in rapidly expanding firms whose investment and increased sales drive waves of economic growth, as with the entire package of petroleum-fuelled, mass-produced automobiles or consumer durables more generally. The table III.1 details the history of growth waves, including a speculative "sixth" wave.

Table III.1
Six Schumpeterian technological revolutions and growth waves

	FIRST WAVE	SECOND WAVE	THIRD WAVE	FOURTH WAVE	FIFTH WAVE	SIXTH WAVE
Developing economy effects	Intensification of enslaved labour and sugar exports	Transition from coerced to indentured and wage labour	Agricultural commodity boom	Import substitution era	New international division of labour, new agricultural exports	New emerging trends (see discussion in the text)
Financial innovation	Small private banks and local networks (e.g. the Quakers in the United Kingdom, notaries in France)	State investment subsidies and public debt	Corporations and open capital markets	State investment subsidies, public banks, segmented financial markets	Venture capital, securitization, institutional investors	Private equity and private debt, overt State industrial policy subsidies
Transport mode	Canals	Railroads	Steamships, urban trams and bicycles	Cars, trucks and airplanes	Telecommu-nications and containerization	Electrified vehicles
Energy source	Water	Coal, gas	Fossil fuel, electricity	Fossil fuels	Fossil fuels	Renewables
General-purpose technologies	Factory production	Metal machinery	Bessemer and open-hearth furnaces; continuous flow production	Continuous flow assembly line	Semiconductors and software, Internet, bioengineering	Artificial intelligence, nanotechnology, bioinformatics
	1771	1829	1874	1914	1970	2020
	Industrial revolution	Railroad wave	First globalization era	Automobile wave	ICT wave and second globalization era	Potential sixth, techno-scientific wave

Source: UNCTAD based on Schwartz (2019).

Note: General-purpose technology encompasses technologies general enough to be used in various industries and with a strong impact on their functioning, given their potential for technical improvements and complementarities for innovation.

These growth waves positively and negatively shape the potential for using exports as a development engine. Positively, a new growth wave almost always increases demand for developing country exports above the current trend level. For example, the emergence of the bicycle and automobile industries in the late nineteenth century vastly increased demand for South-East Asian rubber and Balkan mineral exports (Lewis, 1970; Berend and Ranki, 1977). The proliferation of ICT goods created a niche for labour-intensive assembly in East Asia. In both cases, foreign and local actors created new production zones and export streams. These potentially generated local development as backward and forward linkages emerged, and as the corresponding increase in local aggregate demand induced more production for local consumption. Today, this kind of potential is visible in the increased demand for lithium and battery-related rare earths generated by the shift to electric vehicles (UNCTAD, 2024a).

In a second positive effect, the emergence of new growth sectors in advanced countries has often led to shifting older manufacturing sectors to developing countries, as in Akamatsu Kaname's "flying geese" model (Bernard and Ravenhill, 2011). Greater productivity in new sectors enabled higher wages in developed economies, which pushed less-productive sectors offshore in search of lower wage costs. The "flying geese" model captured a dynamic that was more common before the 1980s, namely, the shift of entire industries from developed to developing countries (UNCTAD, 1996). A classic case was the relocation of garment assembly and eventually mass-produced textiles, from, for example, Japan to the Republic of Korea, from the Republic of Korea to China, and eventually from China to, among others, Ethiopia.

This shift was uneven. Not all developing countries benefited, and a subtle change occurred after the 1970s. Rather than entire industries moving, multinational enterprises allocated selected slices of their production processes to developing countries, seeking to optimize wage and productivity levels, skills and logistics costs (UNCTAD, 2002, 2003). Roughly two thirds of global trade involved intermediate goods, indicating a relatively significant degree of decomposition, particularly in the highly globalized automobile, clothing and electronics industries (Lund et al., 2019).

Financing for this shift was uneven with respect to the implications for the control and funding of companies. In the immediate post-war era, a handful of developing economies self-financed the roll-out of consumer goods production and some capital goods production. Development banks and aid largely provided relatively small volumes of external finance, often tied to purchases from donor economies. In both cases, public rather than private authorities controlled the sources and disposition of capital (e.g. UNCTAD, 1998, 2016).

In the 1970s, the removal of capital controls in developed countries and the recycling of petrodollar surpluses unleashed a flood of cross-border lending from privately owned banks to State financial companies in developing countries. While this seemed to free these economies from the financing constraints of the 1960s, it also exposed them to the vagaries of monetary policy changes in the advanced economies. The legacy of the debt crisis in the 1980s induced a desire to shift towards local currency-denominated debt, which some developing countries realized in the 2010s (Onen et al., 2023).

At the same time, companies from developing countries ventured into global capital markets to borrow in harder currencies (Glen and Pinto, 1995). This shift was largely complete by the 2010s. This period also saw a growing degree of passive ownership of larger developing country firms by advanced country institutional investors. Generally, shifts in financing modes that first emerged in developed countries arose later or not at all in the developing world. By 2011, among the top 500 asset managers

The mix of private and State ownership in developing economies may foreshadow a global trend.

across the world, only 36 were from large developing economies, namely, Brazil, China, India and South Africa (Towers Watson, 2012; Celik and Isaksson, 2013). That said, the combination of private (unlisted) and State ownership prevailing in developing economies possibly anticipates the broader global shift towards State ownership and sovereign wealth funds (Babić, 2023; Babić et al., 2023).

The global decomposition of production greatly affects how countries can respond to the major changes caused by the emerging sixth Schumpeterian growth wave. Some medium-technology industries will shift to some developing economies, although the lack of product differentiation and low barriers to entry can depress prices. Component production for multinational enterprises, however, might disappear as new products and production technologies displace older ones. Some estimates suggest that only about 18 per cent of global trade in the 2010s was based on labour cost arbitrage, defined as trade with countries where GDP per capita was only up to one fifth of that of its trading partner (Lund et al., 2019: 8).

Only about 18% of global trade in the 2010s was based on labour cost arbitrage.

The ongoing shift towards the "servitization" of manufacturing appears to confirm these trends. With services enhanced by rapid technological advances over the past 20 years, the share of investment in services activities within manufacturing industries has nearly doubled, from 38 per cent in 2003 to 69 per cent in 2023. Today, it represents the majority of foreign direct investment projects. The obvious corollary of rising investment in services is the steep decline in the share of investment in manufacturing activities, which halved, from 26 to 13 per cent, during the same period (UNCTAD, 2024b).

The end of Schumpeterian growth waves has often triggered enormous disruption, such as when entire raw materials export production sectors collapsed or faced sharply falling relative prices, as with guano after the 1909 Haber process began making artificial fertilizers. Similarly, and more relevant to the current inflection point, innovations creating synthetic replacements for raw materials could cap the rate of growth of commodity export volumes and values, as with natural and synthetic rubber. Cardoso and Faletto (1979) meticulously traced the effects of sequential resource export booms in Latin America, showing whether and how different societies were able to use those resource booms to generate local economic diversification and development in the sense of both their economies and State-building.

The more recent dispersion of manufacturing has often involved the transfer of highly codified production processes with little potential for learning by doing or the capture of enough profits to fund a broad programme of local industrialization. Amsden (2001) presents a more optimistic account of manufacturing-led development, albeit before the rapid expansion of Chinese exports globally. These geographic shifts are not necessarily permanent, however.

The "servitization" of manufacturing: A challenge for developing countries

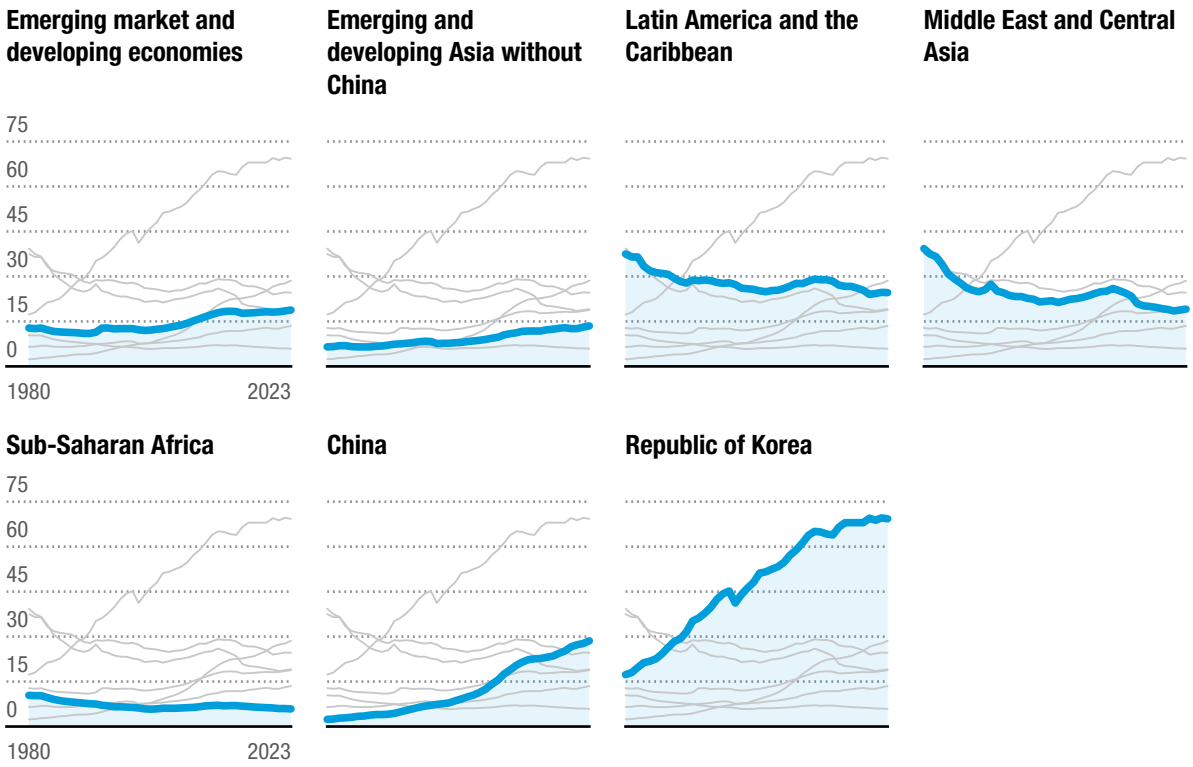
Share of investment in manufacturing industries

While incomes rose, convergence with developed economies remained limited to a few developing countries over 40 years.

Giant companies largely determined what was produced and where, and thus what was exported. Their rubric matched local wages to local productivity, local firms' internal capacity to design and produce components, and the size of the local market (Dunning, 1970; Fröbel et al., 1980; Gereffi et al., 2005). This variously generated full-scale production for local consumption in large, desirable markets such as Brazil or China; production of specific components for global commodity chains, such as automobile transmissions, in countries with mid-level manufacturing skills, including Brazil and Poland; and subcontracted production of various consumer non-durables, especially clothing and shoes, in countries with abundant cheap but disciplined labour, such as Bangladesh or Viet Nam (e.g. Hollveg, 2019).

A handful of countries, particularly in East Asia, climbed up the technology ladder, bringing local incomes and production capacity to something near rich country levels. For example, nominal GDP per capita in the Republic of Korea in purchasing power parity (PPP) terms went from 17.3 per cent of the United States level in 1980 to 69.3 per cent in 2023. By contrast, per capita income in Brazil, which has remained relatively reliant on commodity exports, declined from roughly one third to one quarter of the United States level. Overall, the entire group of developing economies, excluding China, simply maintained a more or less constant sixth of the United States

Figure III.2
Despite exceptions, most countries have not closed gaps in per capita output relative to the United States
GDP per capita relative to United States, selected country (groups)
(Percentage)



Source: UNCTAD based on the IMF World Economic Outlook database (April 2024).
Note: GDP per capita, current PPP international dollars. United States GDP per capita for respective year = 100.

per capita income level in PPP terms, declining from 17.7 per cent in 1980 to 13.5 in 1999–2000, and then recovering to 16.2 per cent in 2023 (IMF, 2023).

As figure III.2 shows, some countries, such as the Republic of Korea and, to a lesser extent, China, dramatically closed the gap with United States per capita income levels, measured in PPP terms. Yet relative per capita income in Latin American and sub-Saharan African economies actually declined; Eastern European countries went back to their pre-transition level; and the rise in both Asian and all developing economies has been largely a function of China's astounding growth. While absolute incomes in most developing economies rose on average over the past 40 years, convergence towards developed economies occurred only in a handful of countries.

The hyperglobalization associated with the fifth, ICT-based Schumpeterian growth wave has effectively created a much more finely grained global division of labour than prior waves. Beyond the ambiguous effects just noted, while the fifth wave opened space for a manufactured goods-led export strategy that prior waves largely lacked, it has potentially locked developing economies into low value added production (Bruhn, 2014; Lectard, 2023). Even the automobile-led fourth wave tended to produce more domestic market-oriented manufacturing sectors behind significant tariff and non-tariff barriers, such as domestic content regulations in automobile production.

The rising proportion of manufactured exports in developing economies over the past 50 years generated productivity gains that were much larger than in prior resource-based export waves. This was because multinational enterprises either brought parts of their own relatively advanced production processes to new production sites or, when subcontracting, helped local firms to upgrade production to a level closer to rich country norms. While multinationals and prime contractors often captured the bulk of productivity gains in the form of cheaper input or wholesale prices, learning by doing and scale effects helped some economies raise local incomes. As Branco Milanović (2016) has shown, income gains in developing countries changed the 1960s bimodal distribution of global income to a more unimodal distribution, albeit with a sharp increase in the very top incomes. That said, the bulk of this income increase occurred in China and developing Asia.

The current inflection point raises questions about what the likely sixth wave will entail, including around whether it will create economic and policy space for export-led development, particularly of manufactured goods.

The fifth growth wave enabled export strategies but locked developing economies into low-value added production.

C. Three critical inflections

Going forward, developing economies are likely to face a radically changed global environment. Three major interacting changes endanger development strategies based on expanded manufactured exports and potentially even resource exports. These changes are a massive shift in market demand and the location of production as a potential sixth growth wave rolls out; the related high risk of deglobalization; and a worsening security environment amplifying deglobalization pressure.

Changing technology, deglobalization, and security issues threaten development strategies reliant on manufacturing and resource exports.

During the last decade, new technologies that could underpin a sixth growth wave have gone from promising to probable. They plausibly comprise the classic elements of a Schumpeterian growth wave. All significantly affect developing country exports and the ability to use export-led development strategies:

1. **New energy sources:** renewables in the form of solar and wind electricity plus geothermal heating. While efforts to generate "negawatts" through conservation will continue, the likely outcome is a huge wave of cheap, renewable electrical energy.

2. **New general purpose production technologies:** bioinformatics, artificial intelligence-enhanced biogenomics and precision biotechnologies. Broader uses of artificial intelligence are less likely to be significant but represent a wild card in manufacturing, particularly through automation.

3. **New consumer products:** a broader range of electrically powered products, including and especially vehicles, and personal transportation options (not just cars but also e-bikes, three-wheelers, etc.), plus new materials through second-generation biotechnologies. There is potentially a shift in consumption towards more personalized medicines.

4. **New transportation modes:** an evolution in the main energy source and thus production process for much of the transportation sector through electrification and a related expansion of developing country personal transport through two- and three-wheel electric vehicles.

5. **New forms of corporate organization:** a factor that is far from clear, but private equity and private debt markets are replacing open capital markets.

6. **New modes of social organization:** the most opaque and unpredictable of all, yet at the same time, the most important, especially in balancing supply and demand at the global level.

Based on obvious interconnections between, for example, new energy sources and transport modes, the following analysis suggests examining these six factors in three sets of paired factors.

1. New energy sources and transportation modes

While it is probably too late to prevent a substantial increase in average global temperatures, policy efforts to decarbonize the economy now work with market forces to promote electrification, in general, and clean transportation, in particular.

A range of countries, advanced and developing, has subsidized emerging solar and wind industries. Prices for wind and solar electricity are now competitive with those for power from coal and in some cases natural gas. This suggests a secular decline in coal use and thus developing country coal exports, which comprised 49 per cent of the global total from 2003 through 2022. Colombia and Mozambique are among the countries that are particularly dependent on coal exports (ITC, 2024).

Further, the electrification of the vehicle fleet portends a massive decline in demand for fossil fuels in general and petroleum in particular (BP, 2023; IEA, 2021; McKinsey Global Institute, 2023). Oil is an even more significant export than coal for many developing economies, including those with relatively high per capita income levels but also high dependence on oil exports. Developing economies accounted for 81 per cent of total world exports of crude oil on average from 2010 to 2022.[15] Demand for petrochemicals and aviation fuels is most likely to continue at current absolute although not per capita levels. But these two sectors jointly only account for about one fifth of global oil demand (BP, 2023; McKinsey Global Institute, 2023). By contrast, demand contraction is already visible for oil consumed in overland transportation, which comprises half the total used worldwide. Global oil production in 2022 was still below its 2018 peak, and major private sector oil firms are disbursing profits to shareholders rather than investing in new production, with spending on greenfield curtailed. Market projections anticipate a sharp deceleration in the growth of global oil and gas capital expenditure from 2024 onwards, compared with the levels seen between 2021 and 2023 (BMI, 2023).

In several developing countries, energy is a large component of exports overall, often dominated by fossil fuels. Table III.2 shows 35 countries where energy exports comprise more than 30 per cent of total exports. For the 25 countries where energy exports constitute more than half the total, the expected permanent negative shock to the value of exports (including through prices) is projected to have a significant impact.

Energy exporters with substantial accumulations of past fossil fuel export revenues, such as Kuwait, Qatar and Saudi Arabia, may be able to transition into a more diversified economy, as smaller Arab and Persian Gulf States have done. These exporters often have low production costs, which provides a further advantage in a context of expected declining fossil fuel export prices and energy transition. But the scale of this shock cannot be overstated, given that fuel exports comprised about 44 per cent of all global commodity exports by value and 14 per cent of all commodity exports from 2012 to 2022. Based on UNCTAD data, fuel exporters account for roughly one third of the 101 most commodity-dependent exporters.

[15] Calculated based on the Standard International Trade Classification (SITC) of the United Nations, group 333, comprising petroleum oils and oils obtained from bituminous minerals, crude.

Table III.2
Some countries are highly vulnerable to a downturn in energy exports
Developing countries with energy exports greater than 30 per cent of total merchandise exports, in descending order of shares, 2022

Country	Energy exports (Billions of dollars)	Total merchandise exports (Billions of dollars)	Share of energy exports in total merchandise exports (Percentage)
Iraq	124.8	129.3	96.5
Algeria	57.8	60.9	94.9
Angola	48.1	51.3	93.7
Libya	35.5	38.0	93.6
Nigeria	57.9	63.6	91.1
Azerbaijan	34.4	38.1	90.3
Turkmenistan	11.8	13.2	88.9
Equatorial Guinea	6.6	7.5	88.5
South Sudan	0.7	0.9	84.5
Qatar	109.2	131.0	83.4
Brunei Darussalam	11.4	14.2	80.3
Venezuela (Bolivarian Rep. of)	3.6	4.7	77.2
Saudi Arabia	319.9	426.5	75.0
Guyana	8.3	11.3	73.3
Chad	2.4	3.5	69.4
Gabon	5.8	9.2	63.3
Congo	6.6	10.7	61.7
Kazakhstan	51.8	84.4	61.4
Colombia	35.1	58.6	60.0
Trinidad and Tobago	7.6	13.3	57.4
Oman	37.3	66.5	56.1
Mongolia	7.0	12.5	55.5
Cameroon	3.2	5.9	54.8
Kuwait	51.7	101.3	51.0
Iran (Islamic Republic of)	36.7	72.1	50.9
Timor-Leste	0.2	0.5	49.7
United Arab Emirates	262.1	532.8	49.2
Yemen	0.4	0.9	48.2
Mozambique	3.8	8.3	46.1
Papua New Guinea	5.6	14.5	38.5
Ecuador	11.7	32.7	35.9
Ghana	6.7	18.7	35.9
Lao People's Dem. Rep.	2.7	7.6	34.8
Indonesia	100.4	292.0	34.4
Egypt	15.6	48.1	32.4

Source: UNCTAD based on UNCTADstat export data.

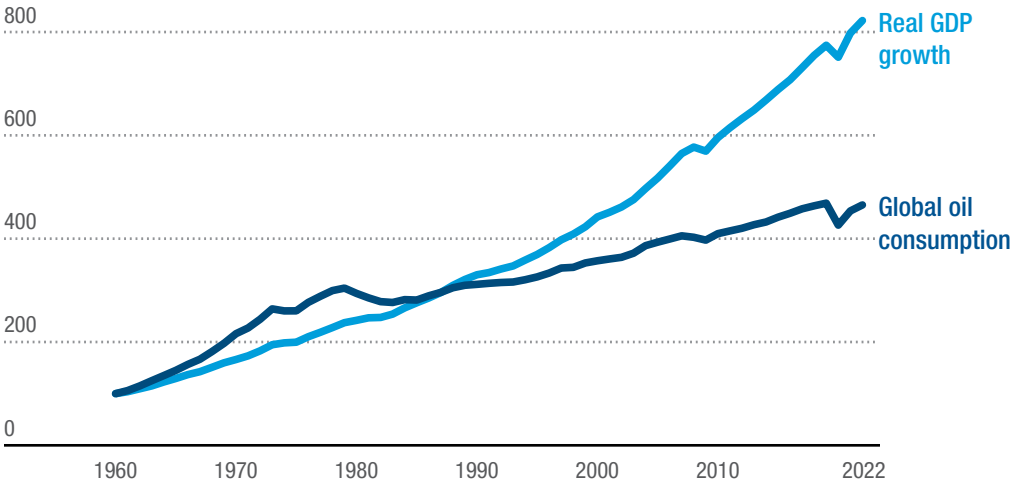
Note: The Bahamas, Jamaica and Saint Lucia are not included as their energy exports are dominated by re-exports. Energy exports from the Lao People's Democratic Republic are mostly electricity.

The growing disconnection between GDP growth and oil consumption that started in the mid-1980s in the developed economies now extends to many developing economies (figure III.3). Unlike the past, when rising incomes in developing countries spurred consumption of petroleum for personal and commercial transportation, future increases will likely be met by electrified light vehicles, especially scooters and very light vehicles. Global car sales peaked in 2017 and are currently below the 2011 level – itself a crisis year. Meanwhile, one seventh of new cars sold in 2022 were electric.

From 2002 to 2021, 8 of the 10 largest oil importers cumulatively were advanced countries with the ability to fund a roll-out of renewable energy (ITC, 2024). The other two were China and India, both of which have committed to expanding solar electricity production and would prefer to reduce dependence on imported oil.

Future increases of demand for personal and commercial transportation are likely to be met by electrified light vehicles.

Figure III.3
The connection between GDP growth and oil consumption has been receding since the mid-1980s
World output compared to oil consumption growth
(Index numbers, 1960 = 100)

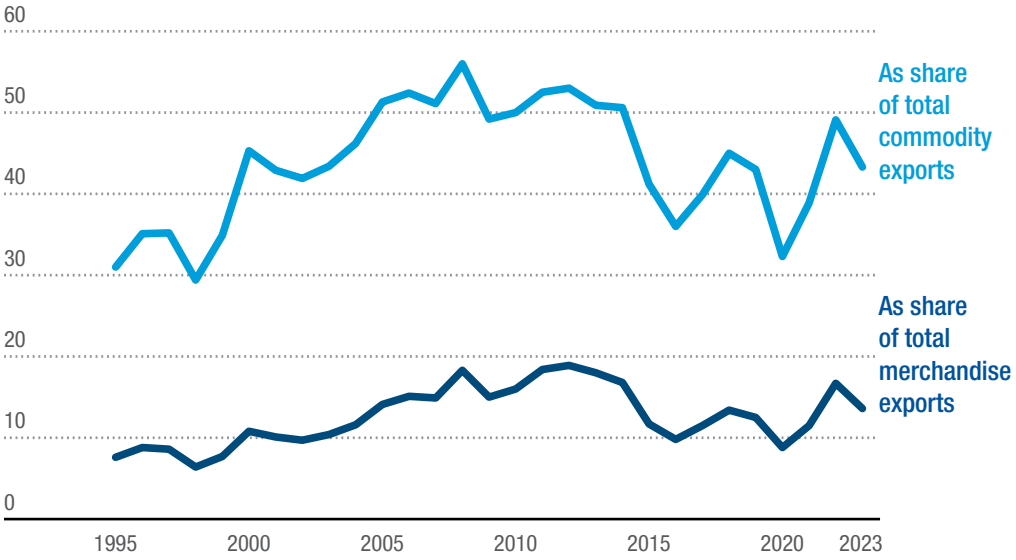


Source: UNCTAD based on the LSEG Eikon database.

Although the large existing fleet of petroleum-fuelled vehicles necessarily slows change, countries that rely on petroleum exports for a substantial portion of export revenues will likely encounter increasing constraints in funding existing import levels over the next two decades. This difficulty will be existential for countries such as Angola, Azerbaijan and Libya, where fuel exports comprised over 40 per cent of total GDP – not just exports – on average from 2010 to 2022, and where past export revenue has been largely consumed.

A second set of countries, where oil exports comprise over 25 per cent of GDP, such as Algeria, the Bolivarian Republic of Venezuela and Kazakhstan could also be affected by this shift. All told, crude oil exports comprise over 30 per cent of exports for 22 developing countries, and over 50 per cent for 14 of those 22. A third group of countries using oil exports to fund consumable imports is likely to find income constrained.

Figure III.4
As the energy transition moves forward, export-dependent countries with high shares of fuels could face a significant shock
Exports of fuels as shares of total commodity and merchandise exports
(Percentage)



Source: UNCTAD based on the UNCTADstat database.
Note: Based on the Standard International Trade Classification, Revision 3.

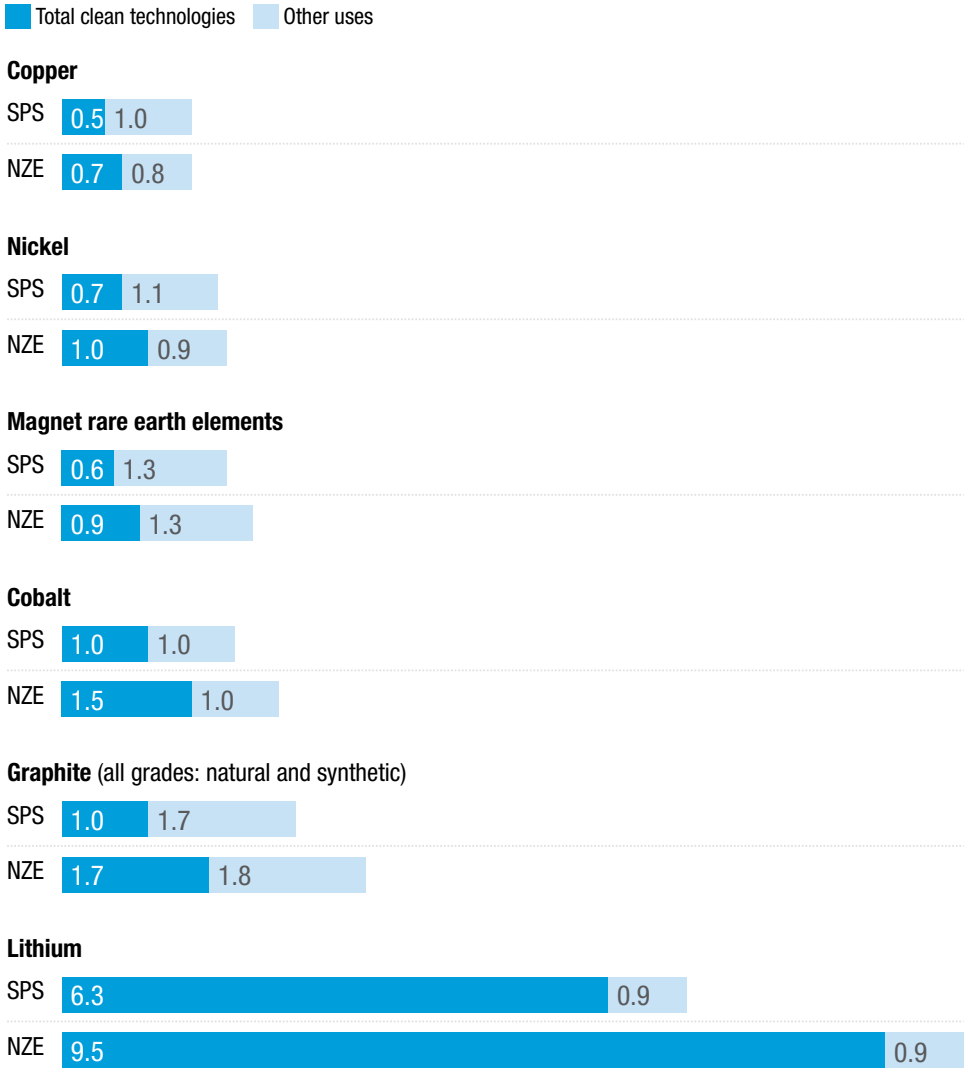
Importing countries aim to secure access to transition minerals, often by ramping up domestic mining operations.

The fact that most developing countries are in locations favouring solar electricity generation might enable them to free themselves from oil imports and the related need to fund oil-import-driven trade deficits with debt. This has important implications for the centrality of the United States dollar in global trade and finance. From 1992 to 2021, roughly one fourth of the cumulative global current account deficit was attributable to net oil imports (IMF, 2023). This deficit required financing, which as a matter of accounting identities was offset by the corresponding current account surpluses of oil exporters. But as oil was and largely still is priced in dollars, net oil importers typically borrowed those surpluses in dollars, even if indirectly. This freed borrowing capacity to import goods for renewable energy infrastructure yet also introduced some uncertainty into trade invoicing, an issue considered in the next section.

Some developing economies will benefit from increased demand for raw materials critical for electrification. According to the latest UNCTAD analysis, the global response to surging demand for transition minerals mainly centres on growing minerals extraction (figure III.5). Importing countries aim to secure access to these minerals, often by ramping up domestic mining operations as part of widespread efforts to bridge gaps between supply and demand. Global exploration budgets rose by 16 per cent in 2022, following a strong 34 per cent rebound in 2021. Latin America was the primary destination of 25 per cent of this exploration in 2022. Africa was second, accounting for 17 per cent (Standard and Poor's Global Market Intelligence, 2023). Investment in critical minerals development rose sharply, by 30 per cent in 2022, following a 20 per cent increase in 2021 (IEA, 2023). It remains to be seen whether this investment will be enough to meet increasing demand (UNCTAD, 2024c: 43).

Figure III.5
Demand for key energy transition minerals is taking off and will likely grow significantly by 2050

Ratio to 2023 demand of the stated policy scenario and a net-zero emissions scenario, both by 2050



Source: UNCTAD based on IEA, 2024b.

Note: SPS refers to a stated policy scenario and NZE to a net-zero emissions scenario, both by 2050.

It is important not to overstate the degree to which demand for minerals can drive development for more than a few countries. Some materials required for renewables, such as lithium, are widely dispersed geographically (table III.3), although processing is currently fairly concentrated. Others, such as cobalt or rare earths, are not. Advanced economies, such as Australia and the United States, are already inducing local production with new industrial policies. Norwegian authorities announced an 8.8-million-ton deposit of rare earth elements in June 2024. Security concerns are reinforcing efforts to find more readily and locally available materials for batteries, such as iron, rather than relying on minerals such as cobalt with concentrated supply sources.

It is important not to overstate the degree to which demand for transition minerals can drive development for more than a few countries.

Table III.3
Geographically, lithium resources are dispersed

Regions	Production		Reserves		Resources	
	Tons (Thousands)	Number of countries	Tons (Thousands)	Number of countries	Tons (Thousands)	Number of countries
Africa	1	1	220	1	4,340,000	5
Asia and Oceania	54	2	6,200	2	11,550,000	3
Europe	1	1	60	1	5,870,000	7
North America	1	1	1,280	2	10,800,000	2
South America	26	3	11,195	3	52,950,000	6
Unclassified			2,045		490,000	

Source: UNCTAD based on data from the International Lithium Association.

New technologies may disrupt markets, affecting trade and stability, while reliance on scarce materials increases risks.

This analysis highlights several risks for developing countries.

1. **First, electrification may reduce the development potential of raw materials exports.** While quantities of some exports may increase in line with population growth, many will likely shrink on a per capita basis in terms of quantity and value.
2. **Second, the introduction of new technologies may disrupt existing markets, impacting trade flows and economic stability.** Dependence on critical and scarce materials for batteries further exacerbates these risks, as their supply chains are prone to disruptions and hence price volatility and shortages.
3. **Third, fluctuations in demand, supply chain issues and geopolitical factors can cause significant price volatility in new energy technologies and transportation modes.** As these technologies evolve, shifts in global economic power and trade balances may affect trade relationships and agreements.

These risks point to the importance of international agreements and mechanisms to help advance the global shift towards more sustainable transportation systems while addressing the complex challenges of the energy transformation (box III.3).

Box III.3
Cars, ships and planes – international policy mechanisms are steering more sustainable transportation

Towards achieving global emissions reduction targets, such as those established by the Paris Agreement, countries often set specific targets for reducing transportation emissions, including in nationally determined contributions. Such commitments have led to policies promoting cleaner transportation technologies and practices.

Greater policy harmonization fosters a unified global strategy for lowering emissions. International agreements urge countries to synchronize transportation policies with global standards, such as fuel economy regulations and electric vehicle incentives, towards expanding markets for clean technologies and cutting costs.

Standards and regulations by organizations such as the International Maritime Organization and the International Civil Aviation Organization help reduce emissions in shipping and aviation. For example, the International Convention for the Prevention of Pollution from Ships includes regulations to limit sulfur emissions and encourage the use of cleaner fuels and technologies.

Financing and investment provided by international mechanisms such as the Green Climate Fund and the Global Environment Facility support sustainable transportation and reduced emissions. Multilateral initiatives should not add to the existing debt burdens of developing countries, however. Vulnerable economies, such as landlocked developing countries, least developed countries and small island developing States, should receive needed official development assistance and financial support to navigate the macroeconomic consequences of potential technological disruptions and the energy transition.

International collaborations drive technology and innovation. The Technology Collaboration Programme and Mission Innovation of the IEA are advancing research on transportation technologies, for example. The Clean Energy Ministerial's Electric Vehicles Initiative and the Global Fuel Economy Initiative promote best practices and fuel efficiency. Regional efforts, such as the European Union's Green Deal, set ambitious targets for collective transportation transitions. International organizations also offer capacity-building and technical assistance for sustainable transportation policies. Expanding multilateral policy coordination to steer such initiatives should avoid disadvantaging developing and vulnerable economies, and support more inclusive global governance based on transparency and fairness.

The private sector can drive progress in new energy sources for transportation by investing in research and development for electric vehicles, hydrogen fuel cells and advanced biofuels. Companies including Tesla, Rivian and Plug Power lead in commercializing these technologies. While private investors invest in start-ups and projects, and businesses play major roles in developing essential infrastructure such as electric vehicle charging networks, the regulation and governance of these new segments is also critical to balance risks and benefits for societies. Public investment programmes and new industrial policies for a green transition can be vital in coordinating the development of new industries. Collaboration among businesses, Governments and research institutions could boost technology development and accelerate the shift to cleaner transportation. Companies could expedite this process by advocating for supportive policies and integrating sustainability into their own operations.

2. New general-purpose technologies and consumer and investment goods

Biotechnologies, bioinformatics, and AI could replace developing countries' exports with advanced economies' local production.

Artificial intelligence-enhanced biogenomics combined with other second-generation precision biotechnologies pose a second substantial threat to export-led development. The reason is simple. From 2013 to 2022, agricultural and mining exports on average constituted over 50 per cent of merchandise exports for 71 of the 155 countries in the IMF group of emerging market and developing economies. Forty-six of the 71 countries are among the poorest countries globally, constituting 58 per cent of low- and lower-middle-income countries under the World Bank's 2022 criterion. Second-generation biotechnologies, bioinformatics and the artificial intelligence-based generation of potentially new materials threaten to replace exports from these countries with local production in advanced economies. Three sets of factors explain the risks.

Data control in precision agriculture means the benefits may not reach most of the world's farmers.

First, agriculture as a whole has been transforming from a labour-intensive activity with irregular yields and long logistical chains to a complex, financialized and digitized system with predictable qualities, scalable quantities and proximity to end-markets. Concentrated corporate control and financialization of the global food system tend to benefit large corporate groups that dominate the market, typically to the disadvantage of producers in the developing world (chapter IV). A few large corporations and financial institutions asymmetrically absorb profits from commodity booms and market volatility (UNCTAD, 2023c).

Within these institutional changes, new technologies and advanced robotics have made digital farming more affordable and accessible. In principle, these shifts can raise efficiency and productivity in agriculture, benefiting farmer incomes and the environment. Yet the digitalization of agriculture could also further accelerate the concentration of plant genome data in the hands of a few large seed companies. Data ownership and control associated with precision technologies in agriculture imply that the benefits, if realized, are unlikely to reach the majority of the world's farmers (Clapp and Ruder, 2020).

Second and related, artificial intelligence-enabled biogenomics and protein visualization programmes[16] allow companies to reverse engineer protein structures. Once a structure is known, DNA and RNA can be precisely constructed to generate proteins, which may or may not be naturally occurring materials. Some advanced country firms[17] have already devised manufacturing processes that produce spider silk analogues, albeit not yet at commercially viable prices. But that qualification indicates an engineering problem rather than some fundamental barrier. Novel biologically based materials are no longer the "unobtanium" of mechanical engineering.

Biologically based products have potential to shift the production of raw materials away from developing countries at the margin. These novel materials could easily displace production of fibres such as cotton on account of their greater strength, wearability and stain resistance (Tummino et al., 2023). In the case of cotton, the pain is likely to be shared across advanced and developing countries, given that roughly 40 per cent of global cotton exports are from the United States.

Overall, about 45 per cent of exports from the 55 most vulnerable countries are agricultural products. As with petroleum, new materials are unlikely to displace all existing production and exports. But they might limit volume growth and put downward pressure on values, which in turn would inhibit the growth of local demand needed to induce manufacturing investment. Developing economies may

[16] See, for example, the Alphafold Protein Structure Database.
[17] Such as Bolt Threads and Gingko Bioworks.

become producers of raw material inputs for new biologically based production processes, but this would consign them to a lower value added segment of the commodity or value chain.

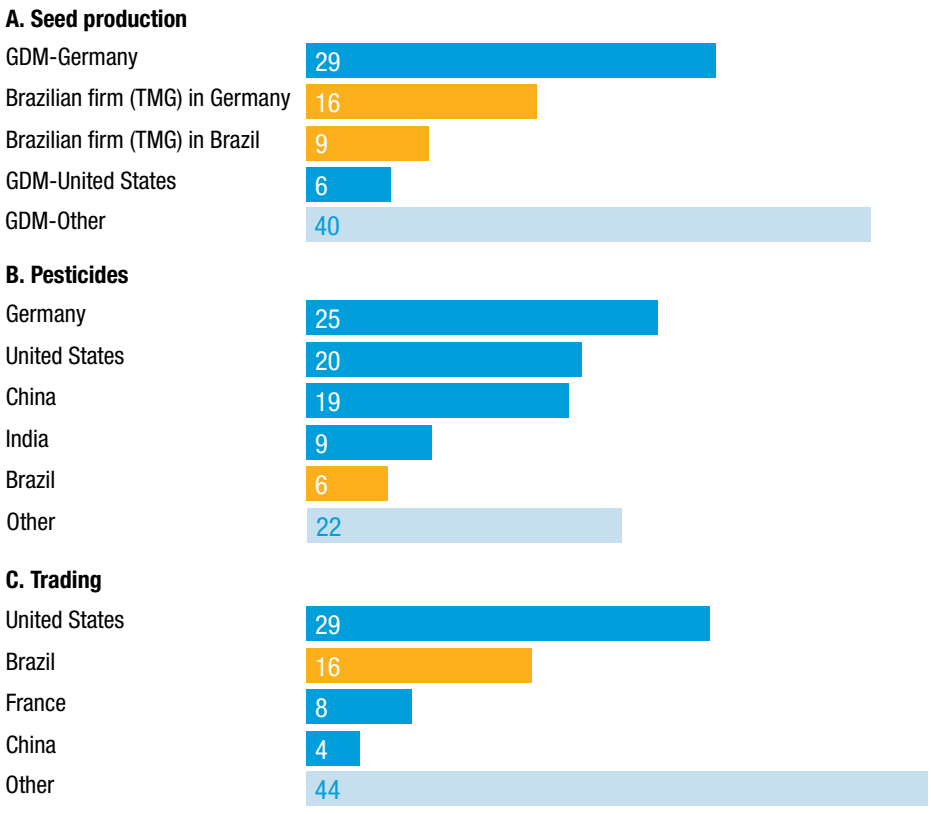
Bioengineering might make it possible to grow some tropical fruits and vegetables in temperate climates, particularly in so-called vertical farming structures. It also may expand the range of agricultural goods produced in developing economies through land-intensive methods, whether for export or domestic consumption. The historical record, however, suggests that developed country owners of intellectual property related to these novel goods or necessary inputs tend to capture the bulk of revenue generated (Dosi and Stiglitz, 2013).

Some developing economies have managed to overcome this problem. The engineering by Brazil of soya beans suitable for local soils is one such example. But most developing countries are unlikely to have this country's research capacity. They may struggle to face the giant firms dominating food processing and agrichemicals (Baines, 2017). Even Brazil has difficulty capturing the bulk of revenue from its soya bean commodity chain. Medina and Thomé (2021) estimate that it gains only 36 per cent of total profits, given its near total dependence on foreign firms for tractors and combines, seeds and marketing, along with lesser but still significant dependence on foreign-made fertilizers and pesticides (figure III.6).

Brazil, a top agro-exporter, captures just 36% of soy profits, relying heavily on foreign equipment and seeds.

Figure III.6
Brazil: The soya bean commodity chain loses much of its value through continued dependence on inputs from foreign firms

Selected components of the soya bean supply chain in Brazil, 2020
(Percentage)



Source: UNCTAD based on Medina and Thomé (2021: 63).

Notes: Only two firms are active in the Brazilian market for soya seed production, which enables showing the country- and firm-level market composition. The number of firms active in Brazilian pesticides and trading markets is larger, thus panels B and C only display country-level market composition.

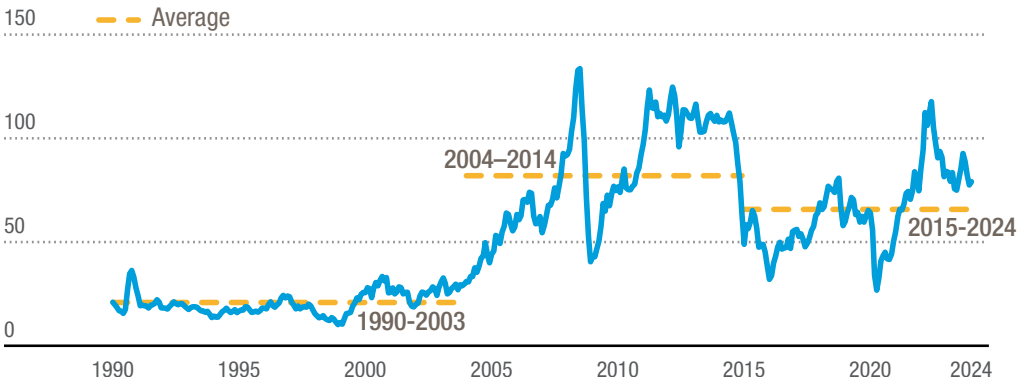
Petrochemical demand may endure vehicle electrification, but plastic pollution drives bio-substitutes, limiting future petroleum exports.

Bioengineered products pose a dual threat to petroleum exporters. First, the bioengineering of crops better able to fix nitrogen is likely to reduce demand for fertilizer, the bulk of which is derived from methane. Rising demand for organic food and agriculture may reinforce this trend. Second, while demand for petrochemicals may survive the electrification of the vehicle fleet, plastic pollution has galvanized a search for biologically based substitutes. As with enhanced crops, this limits volumes and values for petroleum exporters going forward. Plastic is a highly profitable part of the fossil fuel value-chain, as it is derived at very little cost as a refinery byproduct. From a climate perspective, a reduction in excessive plastic use and a move towards non-plastic substitutes is good news.

This step-change presents both policy challenges and opportunities for countries dependent on petroleum exports. A new global treaty regulating plastics is currently being negotiated, including the establishment of a fund for supporting the costs of transition and transformation. Profits could also be made from shifting to non-plastic substitutes. Some countries heavily exposed to plastics are already embracing alternatives, including from seaweed. Not all countries that are fossil fuel exporters are big plastic producers, however; they may even be net plastic importers if they lack necessary chemical plants or refineries. Overall, multifaceted health, economic and environmental benefits come from regulating plastics production, trade and use, and promoting the evolution into less problematic options (Barrowclough and Deere-Birkbeck, 2022; UNCTAD, 2023a).

The combination of artificial intelligence and new additive manufacturing processes is a third threat to exports. Additive manufacturing technologies such as three-dimensional printing enable rapid prototyping and the customization of parts, allowing the production of time-sensitive goods and components much closer to the end user (e.g. Calignano and Mercurio, 2023). The dispersal of labour-intensive, loosely coupled component production by multinational enterprises and of fully built-up consumer non-durable production by retailers made economic sense only as long as logistics and labour costs as well as time sensitivity were relatively low. Logistics costs are approximately 30 per cent of the final cost for goods moved from Asia to the United States or Europe. Such costs can rise if Governments get serious about taxing the carbon content of fossil fuels used for water and air transport. Brent oil prices averaged $24 per barrel from 1990 through 2005, but from 2006 through 2023, they averaged $77 per barrel (figure III.7).

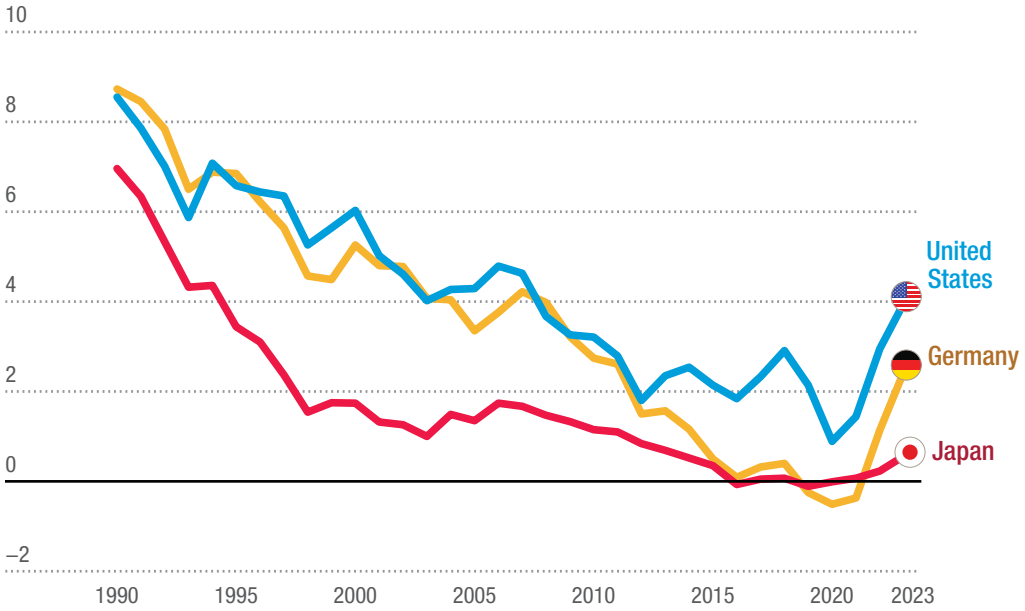
Figure III.7
While lower-cost transport helped drive the dispersal of production, oil prices now hover far above levels in the 1990s
Brent crude oil price per barrel, January 1990–May 2024 (Dollars)



Source: UNCTAD based on United States Federal Reserve System economic data.

While prices did moderate to $68 on average from 2014 through 2023, they remain significantly higher than during the 1990s. In inflation-adjusted terms, using the United States consumer price index as most oil is priced in dollars, oil is now roughly twice as expensive as it was during the hyperglobalization era. Meanwhile, decreased security for water transit has raised insurance costs and transit times for sea routes and some air freight routes from Asia to Europe.[18] Any long-term reversal of the exceedingly low interest rates of the post-2010 era is likely to escalate logistics costs because inventory in the transport pipeline (such as goods in containers on ships) must be financed (figure III.8).

Figure III.8
Higher interest rates on long-term government bonds may lead to spikes in logistics costs
Interest rates on 10-year government bonds in Germany, Japan and the United States
(Percentage)



Source: OECD Monthly Monetary and Financial Statistics data set.

Rising logistics costs incentivize the use of new, onshore production technologies. The so-called third manufacturing revolution – the application of information technology to all phases of manufacturing, and particularly artificial intelligence-enabled additive manufacturing – can lower capital costs relative to wages by reducing downtime, errors and unsold inventory. It may also serve localized markets for highly customized, on-demand products suited to advanced country markets. By putting a premium on design and quality features that are difficult to find and sustain in developing economies, this shift could substitute local production for goods made in distant low-wage labour locations. On the cost side, artificial intelligence will probably increase the efficiency of automation, removing some of the cost of expensive developed country labour from corporate location decisions. In this regard, ILO warns that

Risks of further increases in inequality need to be addressed if the benefits from AI-based technological progress are to be broadly shared.

[18] Based on an UNCTAD rapid assessment in February 2024 available at https://unctad.org/publication/navigating-troubled-waters-impact-global-trade-disruption-shipping-routes-red-sea-black.

risks of further increases in inequality need to be addressed if benefits from artificial intelligence-based technology are to be broadly shared (Ernst et al., 2018).

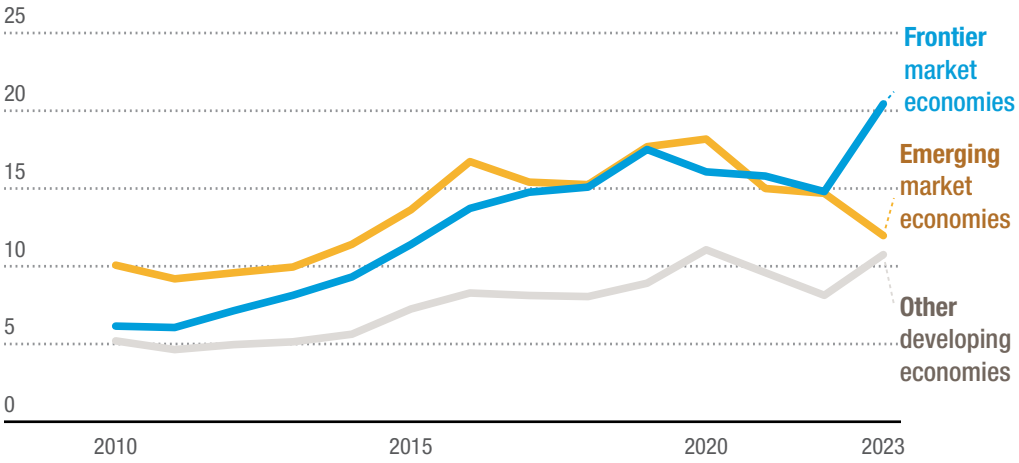
While artificial intelligence in general tends to be overhyped, it likely entails significant negative consequences for labour-intensive offshore services such as telephone-based, low-level technology help and customer service. Routine, codifiable customer service exports are already being handed to artificial intelligence chatbots, decreasing labour demand and thus the aggregate value of such exports (Chang and Phu Huynh, 2016).

New technologies and abundant renewable energy could trigger deflation in primary commodities and undifferentiated manufactured goods.

This shift can be especially hard on providers in India and the Philippines. In 2023, seven of the giant information technology companies of India, including the two biggest, Tata Consultancy Services and Infosys, collectively laid off 75,000 employees or about 4 per cent of their combined workforce (*The Economist,* 2024). Such indicators are mirrored in current shifts in the pattern of foreign direct investment globally, where the share of greenfield investment into high-value-added sectors has grown from 45 per cent in 2004–2007 to 63 per cent in 2020–2023 (UNCTAD, 2024b). This presents formidable challenges for policymakers in low-income countries that are still in early stages of global value chain development.

More broadly, the uptake of new general-purpose technologies combined with potentially abundant renewable energy might spark an era of deflation for many primary commodities and undifferentiated manufactured goods. This is likely to generate two financial problems for developing economies. First, it can reduce export revenues and slow aggregate demand. In turn, this can hinder local investment and global demand for investment goods. Second, falling prices for exports imply less revenue to service debts with the interest and principal fixed in nominal terms (figure III.9). This can intensify stress from external debt on both the macroeconomic balance and, again, local aggregate demand. If left unaddressed by policymakers, these two forces are likely to combine into a cascade of complex, system-level crises, akin to the lost decade that Latin American and other countries experienced in the wake of the 1982 debt crisis.

Figure III.9
Rising external debt servicing relative to export revenues could provoke cascading crises
Proportion of export revenues spent on debt service by type of economies
(Percentage)



Source: UNCTAD calculations based on World Bank International Debt Statistics and the IMF World Economic Outlook.

Summing up, any broad implementation of sixth growth wave technologies – keeping in mind too that climate change considerations could accelerate the energy shift – threatens to reduce major sources of export revenues for developing countries. This process might impede the traditional path to economic development, since exports are critical in addition to local aggregate demand. While not all features of this technological revolution are negative, most are for developing economies. Reducing current debt burdens is thus vital for enabling their financial sustainability in the changing economy.

The discussion above largely left aside geopolitical factors that will be discussed in section D; these too are largely negative.

3. Corporate and social organization

Earlier editions of this report in 2017 and 2018 examined some likely impacts of digitalization on the international organization of production and employment. In 2018, the report suggested that digitalization may reduce dominance by lead firms and shift relationships away from captive governance towards more relational and modular types. Increased possibilities for product customization could move the control of value chains towards customers, whose specific desires for product functionality and features could guide design and production patterns.

Reaping these benefits, however, crucially depends on a supplier's digital capabilities. This is because digitalization also satisfies demands for more granular financial and managerial control and contributes to greater flexibility for lead firms in choosing among an increased number of suppliers. This could heighten the risk that producers without digital capabilities could be marginalized or excluded (UNCTAD, 2018: 76). In this respect, the example of the digital public infrastructure of India (India Stack) highlights the role public policy can play in enabling countries to capitalize on the benefits of digital ecosystems (Alonso et al., 2023).

Despite growing research on the effects of digitalization and artificial intelligence, corporate organization remains an unobvious and unpredictable part of the emerging sixth growth wave. Social organization is, if anything, even less obvious, along with the outcome of diverse political and social struggles in different countries, but Perez (2002) and Schwartz (2019) provide some historical examples. That said, the ongoing turn towards stronger antitrust and anti-monopoly stances in the United States and Europe, in the face of the growing power and size of multinational enterprises (Babić, 2023; Babić et al., 2023; Wang, 2015; UNCTAD, 2023c), points to a challenge to the shareholder-owned, public equity market-based, large-firm model prevailing after 1990. Some new forms of corporate organization are also discernible.

First, in principle, technological imperatives should shape corporate organization to a degree (Kitschelt, 1991). Heavy industry cannot be run by small firms; biotechnology research seems better suited to small, independent teams. In practice, however, institutional mimesis – the human desire to try to emulate what seems like obvious forms of corporate organization (Dimaggio and Powell, 1983) – remains, regardless of technological imperatives. An issue crucial for development is that most companies are enmeshed in complex commodity chains. The nature of their linkages determines the distribution of value generated (see also chapter IV).

For example, consider the difference in profit per employee at Apple, Taiwan Semiconductor Manufacturing Co. (TSMC) and Hon Hai (the parent of electronics assembly giant Foxconn). In this commodity chain, Apple possesses significant intellectual property rights in the form of design patents and software copyrights. TSMC possesses tacit production knowledge and a huge investment in

Sixth wave technologies and energy transition threaten developing countries' exports, making debt reduction crucial for sustainability.

Stronger antitrust policies in Europe and the United States challenge the large, shareholder-owned firm model dominant since 1990.

physical capital for producing the key processing chip going into the iPhone. Foxconn marshals over 1 million workers in China to assemble the iPhone and other electronics. While Foxconn brings significant production knowledge to the table, it relies on key machinery owned by Apple to attain Apple-level quality for fit and finish (Satariano and Burrows, 2011). Consequently, Apple generated €465,451 in cumulative profit per employee from 2004 to 2022, TMSC €257,919 per employee and Hon Hai only €12,984.[19]

Private equity is displacing public firms in advanced economies, while State ownership dominates in developing economies.

Second, with respect to institutional emulation, two somewhat different models seem to be emerging. Both involve some degree of absentee ownership, in which a holding company model and firms appear to be disposable collections of assets. In advanced countries, private equity (Appelbaum and Batt, 2014) and institutional ownership (Braun, 2022) are on the rise, displacing traditional publicly listed firms (Feldman and Kenney, 2024; Murugaboopathy and Oguy, 2022). In many developing economies, State ownership through sovereign wealth funds or, in a reprise of the old Gerschenkron model, State-owned banks seem to be the emerging model (Babić, 2023; Babić et al., 2023; Wang, 2015).

While these changes may not seem particularly important relative to the roughly 25 to 30 per cent GDP share of publicly listed firms, the private equity share has been rising and the publicly listed share falling for the past 30 years (Schlingemann and Stulz, 2022). The private equity (as distinct from private ownership) share of GDP in the United States grew to roughly 6.6 per cent in 2022 (Ernst and Young, 2023). Although private equity is less important outside the United States, the share of equity market capitalization intermediated through the United States and other institutional investors has been growing, as has the presence of private equity firms.

Third, there are signs of a reversal in the vertical disaggregation characterizing corporate structures from the 1980s to the present. After the 1980s, many firms, including and especially in the United States, spun out some labour-intensive and physical capital-intensive activities to concentrate on "core activities" (Pralahad and Hamel, 1990) that were often very human capital-intensive.

The paradigmatic but not unique firm here would be Apple. Apple used to manufacture its own products in its own factories. But from the mid-1990s onwards, it has largely only designed software and more recently semiconductor chips. It subcontracted the production of chips and other physical components going into its products to a variety of Japanese and European firms, and then had components assembled by labour-intensive firms in Asia. Lately, however, Apple is increasingly absorbing what used to be discrete components into its internally designed central processing unit, the brain of the computer. While this is not full-scale vertical reintegration, it does reverse the earlier trends insofar as it brings the production of value in-house. Apple also exerts considerable surveillance and control over its assemblers and some component producers in a kind of de facto reintegration.

Similarly, Chinese automobile producer BYD has returned to the comprehensive, vertically integrated model of vehicle production that used to characterize automobile firms in the 1960s and 1970s. Other car makers are taking stakes in or establishing battery producers, suggesting that reintegration is an emerging phenomenon in the critical vehicle sector. These examples reflect a general process of reconfiguring global value chains towards less complex and fragmented structures in the quest for security and resilience (UNCTAD, 2024b, 2024c).

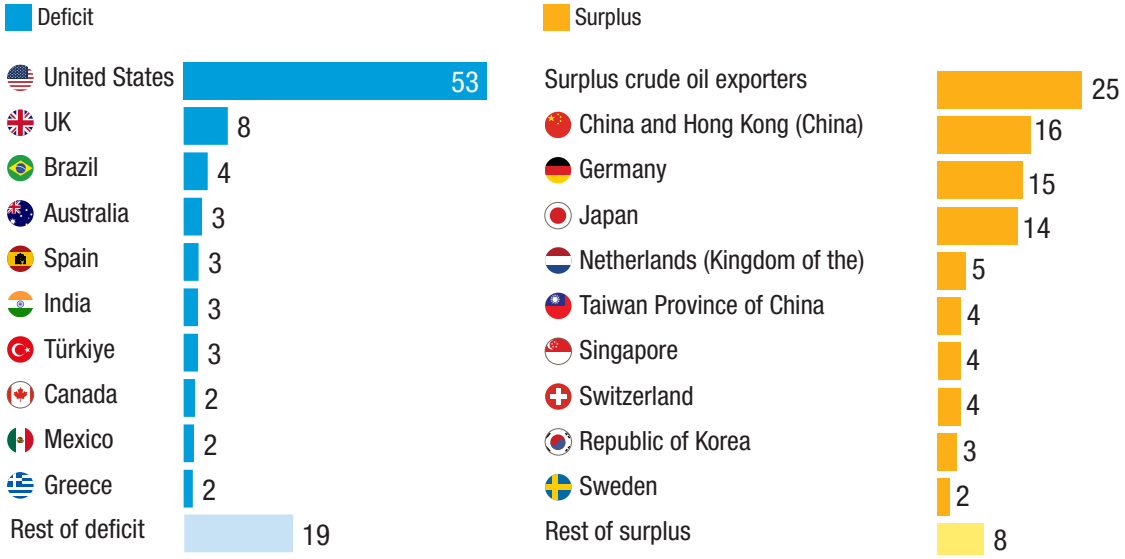
Visualizing the potential social and political institutions that might bring supply and demand into balance is even more difficult.

[19] Calculated based on data from the European Union Economics of Industrial Research and Innovation Directorate available at https://iri.jrc.ec.europa.eu/data.

This is particularly so at a global level, given the difficulties involved in any large-scale multilateral agreement. Few such negotiations have succeeded since the inconclusive WTO Doha Round. Still, persistent global imbalances (figure III.10) driven by supply and demand imbalances at the local level in key economies will put considerable pressure on global institutions regulating trade and domestic politics in both net-exporting and net-importing economies. As Michael Pettis (2024) has argued, the three big non-oil surplus countries all repress wages relative to underlying productivity or repress demand across the whole economy.

Figure III.10
Global imbalances in supply and demand will pressure both trade and domestic politics

Share of cumulative current account deficits and surplus allocations, 1992–2022
(Percentage)



Source: UNCTAD based on the IMF World Economic Outlook Database (April 2024).

Note: Surplus crude oil exporters are Algeria, Angola, Azerbaijan, Bahrain, Brunei Darussalam, Ecuador, Gabon, Iran (Islamic Republic of), Iraq, Kuwait, Libya, Nigeria, Norway, Qatar, Russian Federation, Saudi Arabia, United Arab Emirates and Venezuela (Bolivarian Republic of).

That said, the significant gap between the supply side and domestic demand in key net exporters is increasingly unsustainable, although for oil exporters this is, as noted above, a more complicated situation. Put simply, the top 10 net merchandise exporters, including oil-exporting Norway, the Russian Federation and Saudi Arabia, accounted for roughly 77 per cent of cumulative global current account surpluses from 1992 to 2022. Virtually all have continuous, not just continual, surpluses over that period, indicating structural rather than conjunctural surpluses. And all had household final consumption shares of GDP well below the global average, indicating some degree of repressed domestic demand. Over this extended time period, some surplus countries had household final consumption shares in the range of 30 to 50 per cent of GDP.

The reason to focus on surplus countries rather than deficit ones is that adjustment towards more consumption in the former is less deflationary for the world economy than a reduction of consumption in the latter. The mismatch between supply and weak demand might increase if recent national efforts to expand local supply through industrial policy are successful. This leads to the final challenge for development models built on exporting, namely, the inflection point in the global trade regime.

> Global imbalances may grow if national efforts to boost local production through industrial policies are not paralleled by an increase in demand.

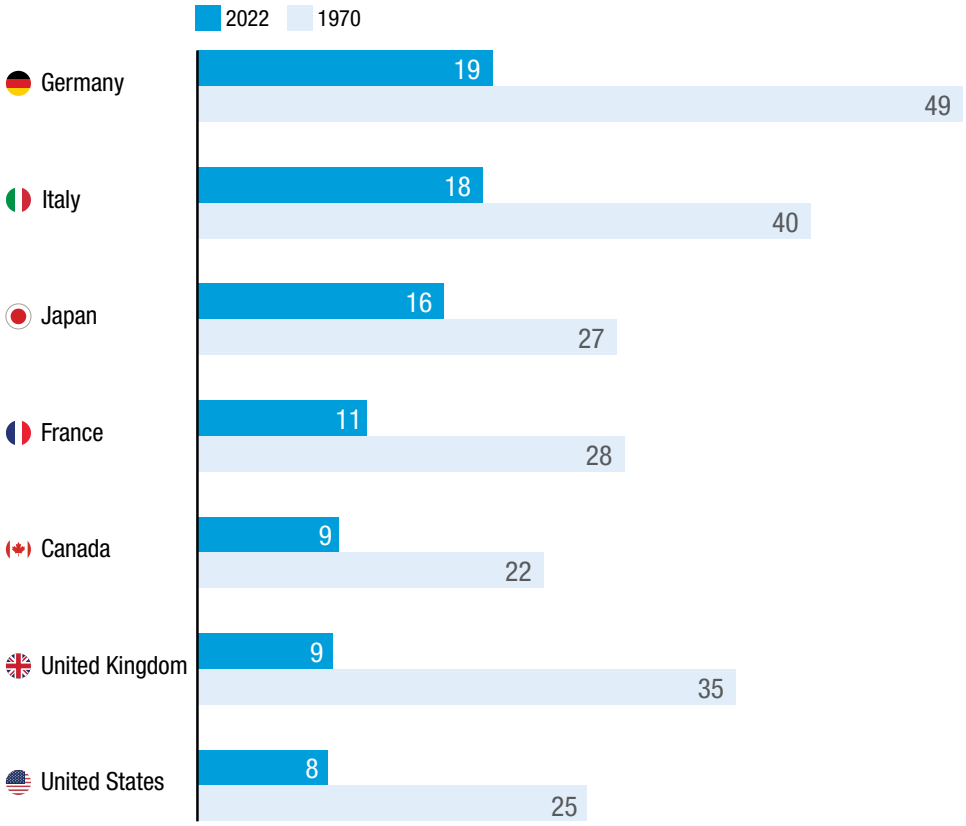
The erosion of rewarding manufacturing jobs, or perceived impossibility of such jobs in the future, have fed fears of economic insecurity rooted in the fragility of livelihoods.

D. Understanding the drivers and effects of a fragmenting trade system

Trade fragmentation can be defined "as a policy-driven change in global trade flows and rearrangement of [global value chains], often guided by strategic considerations" (Gaal et al., 2023: 2). While in the short run, it is easy to ascribe such changes to heightened geopolitical risks, from a longer-term perspective, policy-driven changes to international trade have deeper causes. A range of factors influences the balance of benefits and losses from globalization and, crucially, public perceptions of such a balance. But the relationship between liberalization policies and manufacturing tends to resonate most strongly in political attitudes to trade policies, past and present.

Today, many workers in advanced countries, "having been brought up on the promise of a middle-class democracy underpinned by stable industrial jobs, find themselves toiling in the gig economy" (Galbraith, 2024; figure III.11). The erosion of rewarding manufacturing jobs and the perceived impossibility of such jobs in the future have

Figure III.11
Workers in advanced countries could long count on stable jobs but many no longer find them in manufacturing
Share of manufacturing in total employment, selected developed countries
(Percentage)



Source: UNCTAD based on data from the OECD and United States Bureau of Labor Statistics.

fed fears of economic insecurity rooted in the fragility of livelihoods (Azmanova, 2023).

It is a dangerous trend. In societies where citizens feel disempowered, central authority may grow stronger but also more arbitrary (Azmanova, 2023). This feeds fragility internally and contributes to risks of fragmentation internationally. Trade tensions, protectionism, home-shoring and the securitization of supply chains have become hallmarks of international trade during the past decade. In part, these measures stem from competition and frictions among leading economic powers (China, the United States and the European Union). But new industrial and trade policies also offer a political response to public discontent with the consequences of globalization.

The turn to protectionism in major regional markets adds to existing pressures on the multilateral system. As preceding chapters show, losses to global GDP from economic fragmentation are substantial. Yet when evaluating the potential effects of current tendencies, in the short to medium term, trade (in services and goods) is driven more by demand than changes in efficiency triggered by policies on tariffs and regulation. Trade, as Alan Beattie notes, tends to follow the economic cycle but with a bigger amplitude (Beattie, 2024). It is therefore important not to overstress the extent of deglobalization.

First, outside China and the United States, other advanced economies – such as France and Japan – have increased their openness (Posen, 2021). Second, in absolute terms, global trade and financial flows have continued to grow. In that sense, there has been no deglobalization that might hinder developing country exports.

Yet relative to global GDP, both trade and financial flows are stagnant. Global trade grew twice as fast as global GDP from 1995 to 2007 (Lund et al., 2019: 5). As a proportion of global GDP, however, global trade essentially peaked in 2008 at 16 per cent. As explained in chapter II, despite the rebound in 2023-2024, it remains below pre-pandemic levels. Value added in exports reached its highest level in 2008 and declined through 2022. The pandemic clearly depressed trade even more than GDP in 2020 and 2021 but does not account for stagnating trade from 2011 to 2019. According to World Bank data, for low- and middle-income countries, total trade as a percentage of GDP declined by nearly 8 percentage points from 2008 to 2019. China and India undoubtedly account for much of the drop. But low-income countries saw an even larger 10 percentage-point decline. Further, the ratio of gross to value added exports – a measure of how many times goods and services crossed borders before their final sale – rose from 1.5 in 1993 to a high of 1.9 in 2011 before declining to 1.8 by 2019 (Subramanian et al., 2023: 7).

Policymakers in various developing and some developed economies are concerned about a structural issue: the “reprimarization” of their economies. Reprimarization is the shift from exporting manufactures as part of global commodity chains to exporting raw materials. According to ICT data, in Brazil, for example, raw material exports doubled from 31 per cent in 2003 to 61 per cent in 2022, while manufactured goods exports fell from 38 to 18 per cent.

Trade tensions, home-shoring, and supply chain securitization reflect economic power competition and public discontent with globalization.

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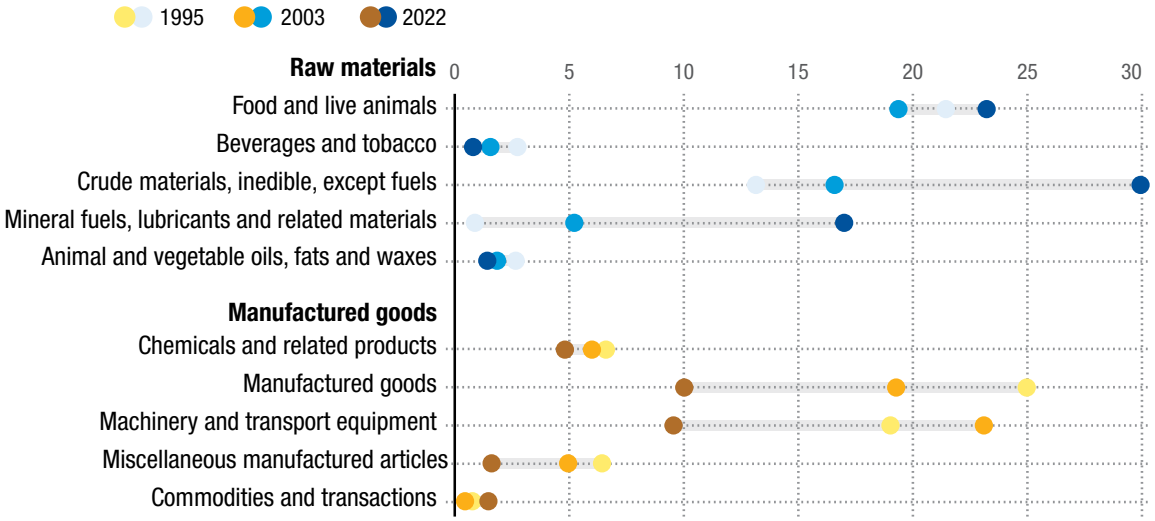
Figure III.12 presents three snapshots of the export mix of Brazil over the last 25 years, showing the growing sophistication of manufactured exports from 1995 to 2003 and then the reversal to minerals and foods after 2003 (see chapter IV for further discussion of the effects of commodity boom). Australia has seen a similar shift from manufacturing to raw materials exports. It seems unlikely that this erosion of manufacturing will be politically sustainable in the long run.

Figure III.12
Wither manufacturing? Brazil's move towards commodity exports
Brazil export mix, 1995, 2003 and 2022
(Percentage)



Source: UNCTADstat database.

Note: Manufactured goods categories include some raw materials items. Relevant in the case of Brazil, non-ferrous metals as well as pearls, precious and semi-precious stones, and non-monetary gold represented between 2 per cent and 5 per cent of the country's export mix between 1995 and 2022.

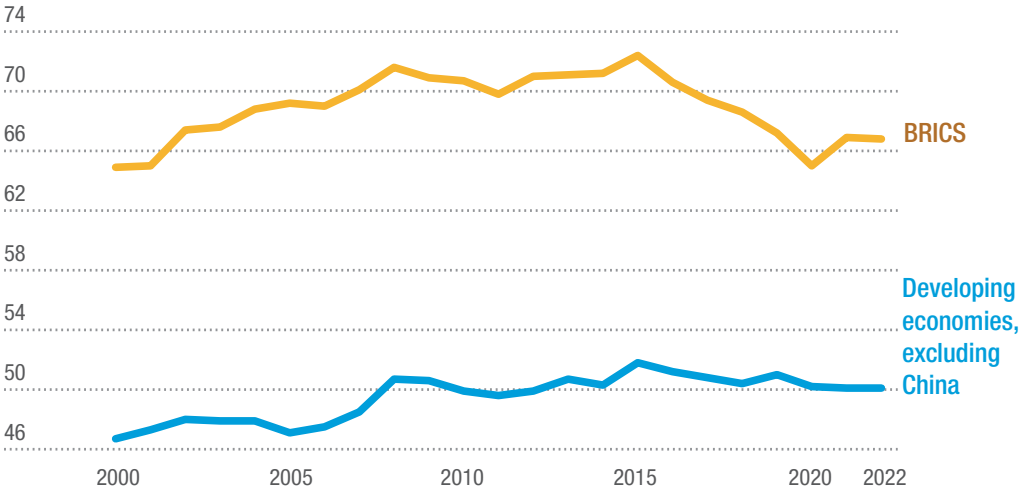
Reprimarization, combined with premature deindustrialization (Rodrik, 2013) shuts off the historic path to development and rising per capita income provided by manufactured goods exports. UNCTAD has long promoted the structural transformation of developing economies from labour-intensive agriculture towards manufacturing and higher value services because this marked the historic rise in income and living standards in developed economies. The capitalization of agricultural production, in both physical and human terms, has reduced agriculture's 40 to 80 per cent share of the labour force to less than 3 per cent in most developed economies today.[20] Workers went into industry and services.

In developing countries, by contrast, informality has increased as agriculture modernized and shed labour, even as industrial employment stagnated or declined outside the BRICS countries. From 1991 to 2022, manufacturing employment rose globally, from 24 to 28 per cent of total employment.[21]

Almost two thirds of that increase occurred in China, however. Brazil saw an essentially flat manufacturing share of employment. Rising informality is one factor contributing to faltering local economic capabilities, as measured by the UNCTAD productive capacity index.[22]

[20] OECD employment data available at https://www.oecd.org/en/data/indicators/employment-by-activity.html.
[21] ILOStat Explorer series available at https://rshiny.ilo.org/dataexplorer37/?lang=en&id=EMP_2EMP_SEX_ECO_NB_A.
[22] The UNCTAD productive capacity index is available at https://unctad.org/topic/least-developed-countries/productive-capacities-index.

Figure III.13
A lack of structural transformation has spurred rising informality and weakened productive capacity
Productive capacity index



Source: UNCTADstat database.

Notes: Structural changes in selected countries. Structural change refers to the movement of labour and other productive resources from low- to high-productivity economic activities. This shift is currently captured by the sophistication and variety of exports, the intensity of fixed capital and the weight of industry and services in total GDP. Higher numbers indicate greater sophistication and development in an economy.

The index of structural change shows a roughly 20 per cent increase in developing economies from 2000 to 2015 but then a slow-down and decline for the BRICS from 2020 to 2022 (figure III.12). Reprimarization is already generating political pressure for trade protectionism, on-shoring and local industrial subsidies. Geopolitical tensions add to pressures to take policy steps that might decrease trade and financial flows relative to global GDP.

This dynamic resembles that of the 1990s, when protectionist measures in the United States against Japan motivated firms to expand electronics and other manufacturing capacity in South-East Asia – but without any capacity reduction in Japan itself. This triggered a short boom era in South-East Asia as investment capital flowed in. But the subsequent surge in excess production caused falling prices, debt servicing difficulties, competitive devaluations and the 1997–1998 financial crisis in the region and beyond.

Global financial flows have also declined secularly. After expanding more than tenfold in current United States dollars from 1992 to 2007 and by ninefold on a per capita basis, the absolute level of foreign direct investment by 2022 had fallen by one third from its 2007 peak and by over two fifths on a per capita basis. While developing economies still experienced growth in foreign direct investment inflows through 2022, these were slowing relative to the era before 2008 and declined absolutely from 2022 to 2023, despite the recovery from COVID-19 (UNCTAD, 2024d).

Similarly, portfolio investment flows fell by 9 per cent from 2020 to 2022, with lending dropping by an even greater 14 per cent.[23] This decline has not been offset by a rise in other type of inflows (chapter II).

Reprimarization pressures and geopolitics drive protectionism, on-shoring, and subsidies, reducing trade and financial flows globally.

[23] Derived from IMF Coordinated Portfolio Investment Survey data available at https://data.imf.org/regular.aspx?key=60587819.

South-South trade, net of trade with China, expanded by almost 150% from 2007 to 2023.

Given that underlying data are in current dollars rather than being adjusted for inflation, the real effect on global growth is probably even greater. Global bank lending has also been stagnant. In constant dollar terms, the stock of outstanding cross-border bank loans is below the 2007 level.[24] The exception is total cross-border portfolio investment, which roughly doubled in real terms from 2008 until the COVID-19 shock in 2020, and then declined in nominal terms by roughly 10 per cent.[25]

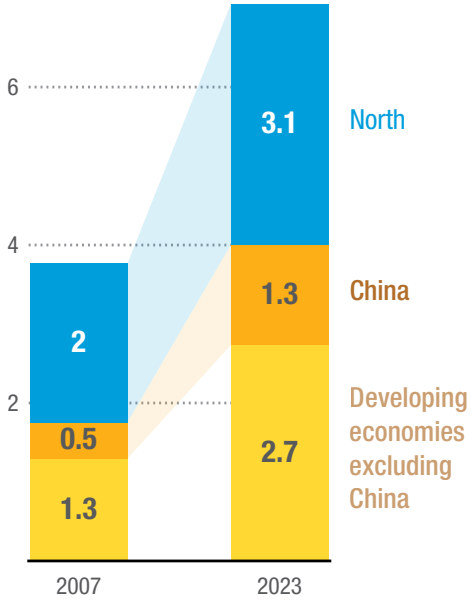
Finally, the economic shock from the United States Federal Reserve Bank's recent increase in interest rates has motivated a search for alternative financing, invoicing and settlement channels. This rate hike resonates with historical memories of the 1982 debt crisis triggered by the bank's similar efforts at inflation reduction. Conventional wisdom sees interest rate increases as a net good, because they tend to strengthen the dollar and make developing country exports more attractive in the United States. But UNCTAD and other recent research (Aldasoro et al., 2018) suggests that rate hikes are a net negative.

A stronger dollar means that local firms in developing economies face a double price shock as the cost of imported, dollar-invoiced intermediates rises, and the interest cost of borrowing to buy those imported intermediates also climbs. Interest rate hikes in the United States tend to reverberate through developing countries' financial markets, depressing economic growth (UNCTAD, 2022, 2023c). Foreign portfolio holdings of developing country sovereign debt, regardless of denomination, declined by 13 per cent from 2020 to 2023 as investors abandoned developing country bonds in favour of higher-yielding instruments in the United States (figure III.8).[26]

The growing degree of South–South trade integration can offset dollar effects (UNCTAD, 2022). South–South trade, net of trade with China, expanded by almost 150 per cent from 2007 to 2023, faster than the doubling of overall South–South trade net of China and of overall global trade growth (figure III.14).

But South–South trade remains largely dollar-invoiced, as most currencies are soft and/or thinly traded. Trade between the global South and China, which has almost tripled over the same period, could be invoiced in renminbi, reducing exposure to dollar exchange and interest rate swings. A shift to renminbi invoicing so far seems largely limited to a portion of oil imports of China and a smaller share of its iron ore imports.

Figure III.14
Exports from the global South almost doubled from 2007 to 2023
Global South exports (excluding China), by trade partner
(Trillions of dollars)

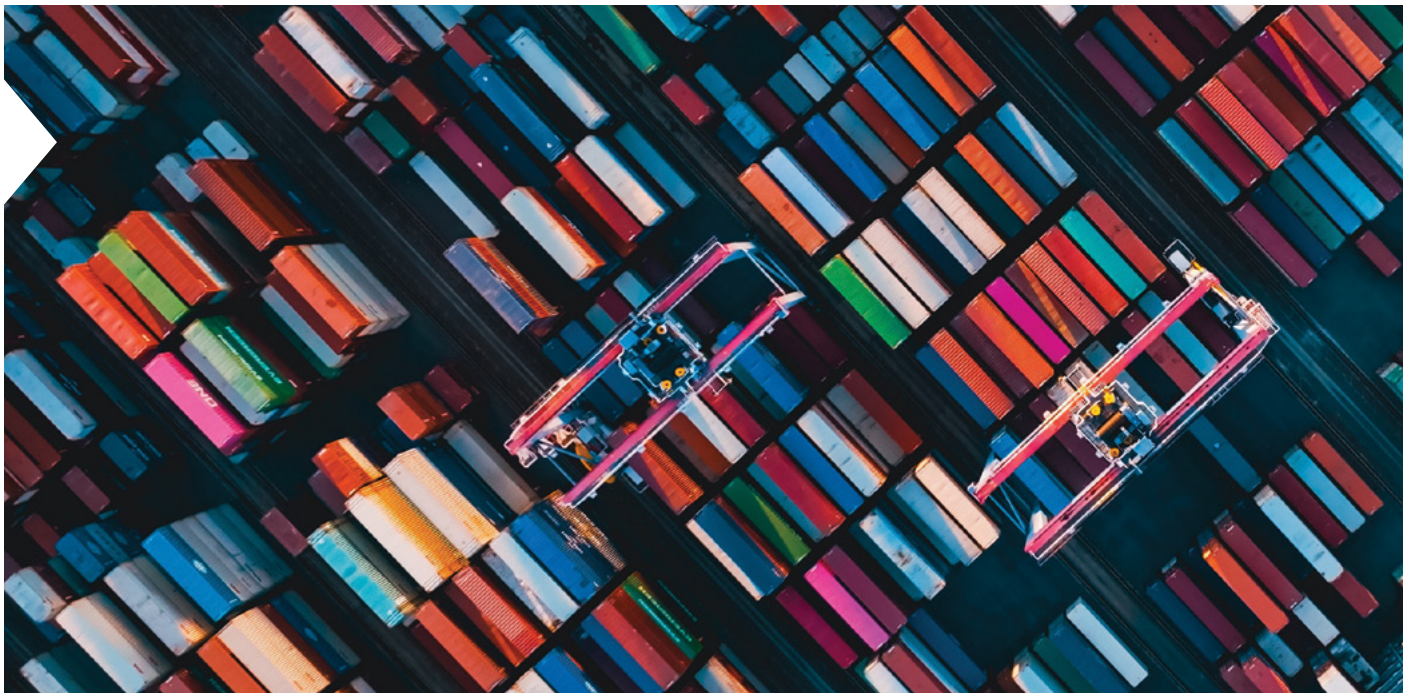


Source: UNCTADstat database.

[24] Based on the Bank for International Settlements BIS Data Portal available at https://data.bis.org/.
[25] Derived from IMF CPIS data available at https://data.imf.org/regular.aspx?key=60587819.
[26] Based on the IMF Sovereign Debt Investor Base for Emerging Markets and Developing Economies available at https://www.imf.org/~/media/Websites/IMF/imported-datasets/external/pubs/ft/wp/2014/Data/wp1439.ashx.

While alternative channels may have beneficial effects by delinking local export invoicing from the dollar and perhaps creating alternative sources of financing, the transition is likely to be fraught. Obvious alternative currencies run into several difficulties. While the currencies of large, well-established surplus economies might seem like a clear choice, in the aggregate, credit creation would require a current account deficit so that borrowers could earn enough euros, renminbi or yen to service new debts. None of the surplus economies is likely to countenance such deficits, however. Globally acceptable synthetic currencies, such as the special drawing rights or a BRICS-based currency, run into similar conflicting interests, hindering renewed trade negotiations.

Alternative payment channels could reduce dollar reliance and create new financing, but the transition will be challenging.



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E. Summary and policy lessons

The current inflection point is not novel. Yet the historical record reveals mixed messages about the geoeconomic and geopolitical transformation of the global economy. Successful development rests on an open trade regime that expands limited domestic aggregate demand, incentivizes and enables industrial investment. That investment, in turn, generates growth and development, understood as increased productive capacity, by means of backward and forward linkages in the domestic economy as well as increased productivity and quality.

New technologies, concentrated in few companies, replace labour and favour home-shoring, heightening governance and policy coordination needs.

A rise in geopolitical tensions and the fragility of the current rules-based trade regime institutionalized in the WTO threaten to disrupt this process. The WTO dispute settlement mechanism is currently not functioning due to vacancies in its appellate body. Such tensions may accelerate rapidly rising South–South trade, enabling growth similar to that powering early industrialization in late nineteenth-century Asia (Abe, 2005; UNCTAD, 2022). The global trade landscape may also provide opportunities for developing countries to bargain for favourable trade, aid and financing conditions.

Geopolitics could accelerate investment in advanced economies in the new, disruptive technologies discussed above. These technologies have complex effects, however, including through the related concentration of corporate control. They are likely to be mostly negative for commodity exporters, though lower-cost electrical power will surely be beneficial.

Exporters of manufactured goods may leverage the artificial intelligence-enabled codification of manufacturing processes to leap forward on productivity, although complementary investment in education and social stability is critical. The subsequent imbalance between production and demand should prompt attention to both the domestic and global distribution of income and thus consumption power.

In short, the developing world today faces challenges similar to those when UNCTAD was first formed. Few observers in 1964 would have discerned the degree to which information and communications technology would help drive globalization and transform the industrial profile of many developing countries. Even fewer would have predicted how the geopolitical tensions of the Cold War would culminate. It is clear that the technological characteristics of the emerging sixth biotechnology and renewable energy wave do not offer a well-defined guide to the next two decades, let alone the next six. Much will depend on the mature management of the stresses on current trade and financial architecture, where geopolitics poses opportunities but could also constrain policy space for developing countries.

Is such management possible? In an ideal world, negotiations in available global forums – the United Nations, WTO, G20, etc. – might help resolve some potential problems from emerging industrial transformation while dampening geopolitical tensions. But the new technological wave is distinct from earlier ones. In addition

to being labour-replacing, as in the past, new technologies are concentrated in a handful of companies. Further, some technologies favour home-shoring.

Governance issues and international policy coordination are therefore increasingly important in three key areas.

1. **First, there is a growing need to ensure greater coordination and coherence among various policies**, including those related to competition, trade, industrial strategy, data protection, digitalization, labour, consumer protection and taxation (see chapter V). More stringent enforcement should tackle the national and international concentration of economic power and control.

   Closing data gaps and innovating more granular methodologies to define the sectoral composition of corporate profits, especially in developing economies, should be a national and international priority.

2. **Second, artificial intelligence needs to be globally governed by agreed principles and standards.** Policies and governance arrangements on precision technologies for agriculture, as one example, are sparse and fragmented. Without legislation, private actors propose codes of conduct or certification schemes (Clapp and Ruder, 2020) that may or may not align to broader development benefits. A delayed or absent political response to the sway of new technologies will likely leave a vast and critical area of the global economy controlled by large corporations and private regulatory bodies. This will be neither inclusive nor necessarily in the public interest.

   The discussion above outlined some major risks facing developing economies. Least developed and landlocked developing countries, small island developing States and African economies are particularly vulnerable to the new technological disruption. At the multilateral level, these countries must have access to resources (ODA, financing for a green transition, debt relief, etc.) as well as technology.

3. **Third and related, many countries have access to self-help policies. But those must be nested inside a greater global trade and investment regime to avoid debilitating trade conflicts and deflation.** Services-export-led growth as a path to development will only remain feasible if new policy barriers are not enacted and access to markets and technologies is safeguarded.

Closing data gaps and developing granular methods to define sectoral corporate profits in developing economies is essential.

Systematic information exchange on existing regulatory frameworks can be a step towards a comprehensive monitoring of global market concentration trends, identifying the economic footprint of multinational enterprises and coordinating international best practice guidelines and policies.

Several self-help policies stand out in developing national policy space. In the potential shift from fossil fuels as the basis for transport and power generation more generally, for example, most developing countries do not have domestic capacity to produce necessary equipment; much will have to be imported. The silver lining is that every incremental increase in renewable energy production should pre-empt or reduce fossil fuel imports. Electrification is not an additional burden in that sense. But as with net oil imports, it requires access to global credit.

For transport equipment, local industrial policy could substitute for imports given that production knowledge is already widely dispersed. Scooters, three-wheeled vehicles and basic transport such as the Bajaj Qute or a revived Tata Nano are more amenable to local production than the electronics-heavy

Delaying political action on new technologies risks corporate control over key economic areas, excluding public interest.

While the 1990s saw the unbundling of manufacturing, the coming decades may see unbundling of services globally.

internal combustion vehicles comprising the bulk of developed country car fleets.

Baldwin and Forslid (2020) suggested that tradable services, particularly those that are artificial intelligence-enhanced, might replace manufactured exports as an engine of demand. Just as the 1990s era of globalization saw the unbundling of and geographical redistribution of manufacturing, the next decades could see an unbundling of services. In some sense, this has already occurred with the relocation of consumer call centres, copyediting and some backend computer services. While this is a trivial example, some restaurants in New York City have begun using Zoom meeting software to have workers in the Philippines take orders and cash out patrons (Chen, 2024). Governments could encourage a similar unbundling of other parts of the services production chain, such as long-distance telehealth, machine monitoring and time-shifted activity.

Yet self-help policies suffer from two defects. First, low-income developing countries are unlikely to execute such strategies as they still lack manufacturing capacity and telecommunications bandwidth. Second, policies promoting extra productive capacity for transport equipment or unbundled services run up against the same fallacy of composition that plagued historical efforts to boost raw materials or basic industrial capacity. If everyone rushes into the same market, prices inevitably fall, and debt service becomes problematic. This will exacerbate the destructive impact of high debt service costs already affecting developing countries, with 19 currently spending more on debt servicing than on education and 45 spending more on interest than on health (UNCTAD, 2024d). International agreements are therefore a necessary complement to local self-help industrial policy. They could guide a range of mostly win–win policies.

First and foremost, the advanced world could live up to existing promises under the United Nations Framework Convention on Climate Change and the Paris Agreement to help fund the energy transition in developing economies (UNCTAD, 2019, 2021b, 2023c). While this inevitably will reduce oil exporters' revenues, it also will help avoid extreme climate changes that impose particularly large costs on their own populations and economies. Many net oil exporters could be encouraged to take advantage of their abundant sunlight to power new industries. Accelerating the energy transition could enable oil importers to meet expanding transportation needs without provoking balance-of-payments problems.

Second, WTO rules on industrial subsidies and trade barriers need to be reconfigured to enable market access and fair competition, and to support raw materials exporters to expand the value added of their exports. Under the existing approach, the effort of Indonesia to induce more local smelting of nickel and chromium ores needed for expanded battery production as well the local production of those batteries stands out as the kind of scenario where WTO disputes are likely to become more common. To the extent that relatively low domestic consumption in export surplus economies stems from the underprovision of domestic public goods, the WTO or similar multilateral agreements could help reduce trade tensions that could potentially spiral into limits on free trade. These kinds of agreements might also spur more South–South trade.

Finally, coordinated policy mechanisms to stabilize domestic agricultural and raw materials production and prices (Schwartz, 2023; Weber, 2024) would help relieve current financial stress and defaults in the global South, largely stemming from higher advanced country interest rates and the potential transition to bioengineered replacements for traditional raw materials. The years of COVID-19 and post-pandemic instability have only increased the need to forge a new global economic compact. It must mitigate mounting geoeconomic and geopolitical challenges and assist countries to navigate the risks of a fragmenting trade system, weak demand and the climate crisis, while achieving the Sustainable Development Goals.

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Chapter IV

Rise, retreat and repositioning: Lessons from the global South

In the early 2000s, the fast-growing economies of the global South appeared as powerful engines of global economic growth. In 2013, the global economy seemed to be divided into a rising South and a crisis-ridden North.

However, the rise of the South had been uneven and incomplete. The commodity boom of 2003–2013 masked structural problems and vast regional divergence.

Global shocks further tested economic resilience of the developing economies. Through all major economic crises of the past 40 years, the South grew faster than the North, but subsequent recessions tended to be deeper.

The regional diversity of the global South raises questions about the direction and type of development strategies today. As the global economy enters a new growth wave, the many earlier assumptions about development models are in doubt, while new challenges emerge.

The success stories of the 1990s may not be easily emulated amid the new commodity cycle, the energy and technology transition, and the advanced financialization and servitization of economies.

United Nations

Key policy takeaways

- **Across the real economy, trade and global value chains, financialization has major implications for integration strategies.** In developing countries, the relationship between financial cycles and commodity prices tends to be pronounced.
- **Managing the expansion and financialization of extractive industries poses a key challenge for commodity-exporting countries** amid the energy transition and a new growth wave.
- **Safeguarding economic resilience requires policy coordination**, including through monitoring the economic footprint of multinational enterprises and sharing relevant data.
- **Finding new pathways to successful development requires re-evaluating the commodity cycle and devising policies** to achieve diversification and redistribution.
- **The balance between the growth of extractive sectors and financialization** needs to be in a focus of policymakers across the global South.

A. Introduction

The early years of the new millennium enriched the international political lexicon considerably. In 2001, Goldman Sachs economist Jim O'Neil coined the term "BRICS" to classify the emerging economies of Brazil, the Russian Federation, India, China and South Africa as an asset class.

In 2009, the BRICS held an inaugural summit and began to formally advance positions on some major issues of global economic governance and intragroup economic priorities (*The Economist,* 2024).

The idea of the rise of the global South emerged in the early 2000s, referring to the fast-growing economies of Africa, East and South-East Asia, and Latin America. This marked their emergence as new, powerful engines of global economic growth. Perspectives on this phenomenon differed, however. Many saw signs of economic convergence between the North and South, noting a shift in global wealth towards emerging markets (OECD, 2014). Yet high rates of economic growth in developing regions and especially their ostensible resilience to the global financial crisis of 2007–2009 contributed to the hypothesis of a "decoupling" between the North and South.

In 2013, the state of the global economy appeared to be a tale of two worlds. One was a resurgent South, most visibly exemplified by countries such as China and India. It was characterized by human development progress, robust growth and rapid poverty reduction. The other was a crisis-ridden North, where austerity policies and recession imposed hardships on millions of unemployed people and pressured social compacts (UNDP, 2013).

In 2013, the global economy appeared to be a tale of two worlds: a resurgent South and a crisis-ridden North.

But it would soon become apparent that the rise of the South was not to last beyond the commodity boom of 2003–2013 (UNCTAD, 2018). After global commodity prices peaked, many developing countries, and especially commodity exporters, retreated into low growth trajectories or stagnated. The end of the commodity cycle exposed persistent structural differences among the economies of Africa, Asia and Latin America. Two major crises, the global financial crisis and the COVID-19 pandemic, as well as the continuing costs of climate change meant that since 2013–2014, the global South began a retreat.

This trajectory is particularly prominent in Africa, the region often seen as a harbinger for the evolution of the global South more broadly (see section B). Following a profound economic crisis that persisted for the last quarter of the twentieth century, from around 2000 onwards, Africa experienced a turning point. Deeper international economic integration brought robust growth and broad optimism about the continent's development prospects. Yet low growth since 2014 and enduring economic and political challenges suggest that African economies did not experience structural transformation during the "Africa rising" years. Since 2014, external shocks, including the pandemic, conflicts, debt and climate crises, have constrained Africa's development prospects.

Does this mean that the global South has peaked as an economic force globally?

Can these countries overcome their macroeconomic divergence to articulate and pursue a shared agenda for the reform of the global economic architecture? What key priorities and challenges do the economies of the South face at the current inflection point in globalization?

This chapter explores these questions. Section B considers key lessons from the initial rise of the global South from 2003 to 2013. Section C examines current policy challenges associated with the continuing financialization of extractive industries. Section D concludes.

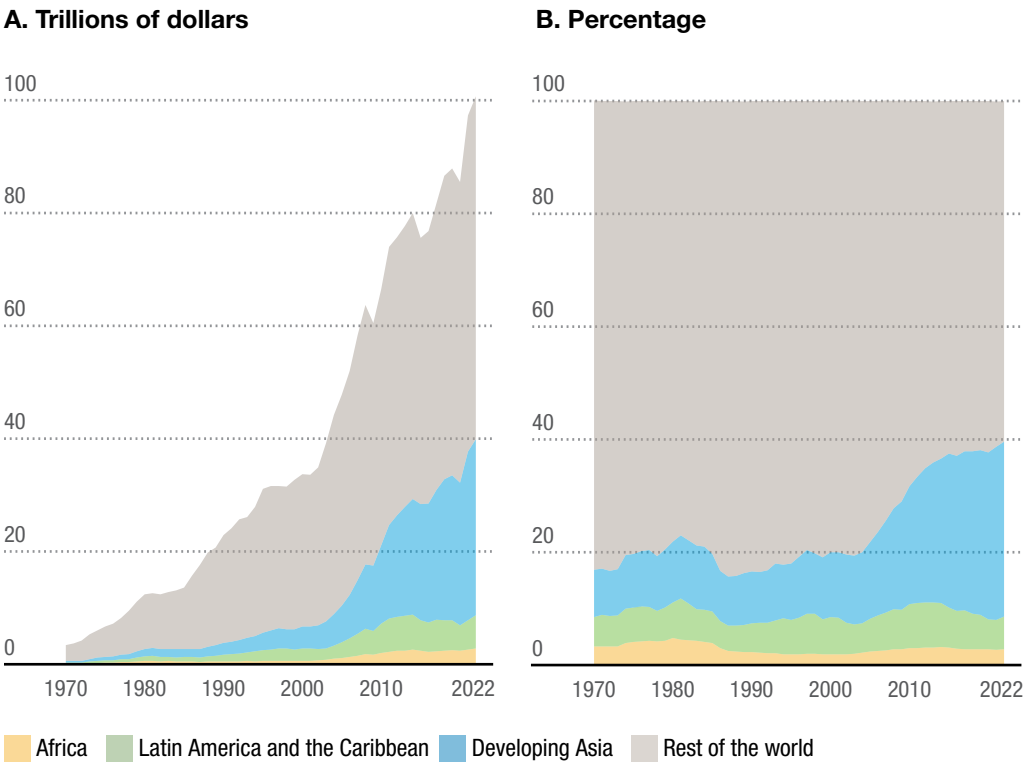
B. The global South: The rise of the idea and the idea of the rise

1. Powers behind the concept

Despite a history going back to the 1960s, the term "global South" has been rather amorphous. It cannot be defined clearly on a map, and it comprises regions and countries with diverse histories, cultures and political-economic regimes. It often refers to the rise of individual countries rather than a cohesive group (*The Economist,* 2024). The boundary between the North and South has not been constant historically, as some economies of the developing South, such as Singapore, have become rich countries themselves (Mold, 2023).

In a wider frame, it is hard to ignore the historic rise of the South since the mid-twentieth century as well as the vast economic potential of developing countries. In the 1970s, together, the developing economies of Africa, Asia, and Latin America and the Caribbean could claim just under 17 per cent of world gross income. By 2022, this figure had risen to nearly 40 per cent, with developing Asia accounting for 31 per cent (figure IV.1).

Figure IV.1
The rise of the global South has brought greater wealth but mainly in Asia
Gross national income, by region



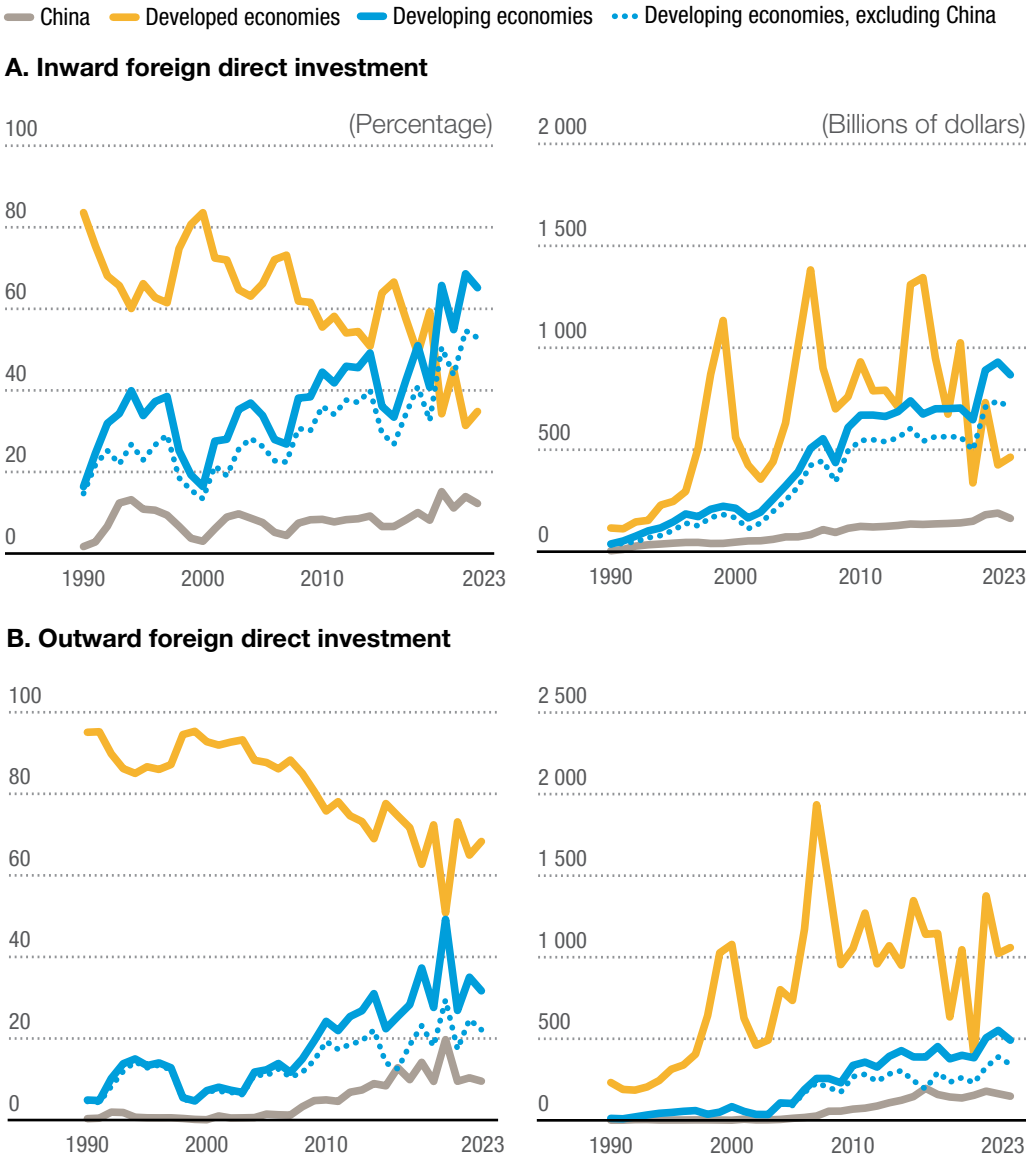
Source: UNCTAD based on National Accounts Main Aggregates database, United Nations Statistics Division.

South–South merchandise trade accounts for around 23% of global trade; the North–North share is 39%.

Today, countries of the global South make up roughly 40 per cent of world gross product and have around 85 per cent of the world's population.

The largest bilateral trade corridor today runs between China and the United States. UNCTAD data shows that South–South merchandise trade accounts for around 23 per cent of global trade; the North–North share is 39 per cent.[27] The global South now hosts more than 65 per cent of total inward foreign direct investment, up from 16 per cent in 1990. In terms of outward foreign direct investment, it accounts for 32 per cent of the total, rising from just 5 per cent in 1990 (UNCTAD, 2024c).

Figure IV.2
The global South hosts more than 65 per cent of inward foreign direct investment
Share of foreign direct investment flows, selected regions



Source: UNCTADstat database.

[27] See https://unctadstat.unctad.org/datacentre/dataviewer/US.IntraTrade.

In light of this economic ascent and amid rising geopolitical tensions since 2022, the global South has regained prominence in the policy vernacular. Leaders in China, France, India and the United States have used it with increasing frequency (*The Economist*, 2024).

The current global South discourse has historical precedents. It is widely believed that Carl Ogelsby, a leftwing writer and activist in the United States, first used it in 1969, remarking that "the North's dominance over the global South…[has] converged…to produce an intolerable social order" (Ogelsby, 1969). While this was not a precise definition of a political grouping at the time, the global South became an umbrella term for countries outside advanced capitalist economies.

During the Cold War, the terms "third world" and "non-aligned countries" were interchangeable in the media, policy circles and academia when commentators referred to political alliances and the security stance of Southern countries. In more specialized discussions of economic and development issues, concepts such as "less developed countries"[28] or "developing countries"[29] were widely used. Since the end of the Cold War, the developing–developed country dichotomy has become widespread and even mainstreamed in multilateral diplomacy. In 2000, the United Nations launched the Millenium Development Goals, which focused on eight development challenges of developing countries.

But the global context kept evolving, and the past decade brought its own revisions of multilateral policy vocabulary. The aftermath of the global financial crisis, the economic rise of developing countries during the first decade of the twenty-first century and the evolution of the BRICS and other emerging economies opened questions, mainly in the North, about the relevance of distinguishing developed and developing countries. In 2015, when the landmark 2030 Agenda for Sustainable Development was adopted, United Nations Member States agreed that the Sustainable Development Goals, the successors to the Millennium Development Goals, should apply to all countries, regardless of development status.

The COVID-19 pandemic and subsequent cascading crises deepened the divide between advanced and developing countries. In tandem, resurging political and security risks reinforced the collective notion of developing economies as the global South. While academic publications have employed this concept since 2008–2009, in the global policy arena, use has exploded only in the past two years. Since 2023, references to the global South have featured in the official documents of the G20, Group of Seven and BRICS summits. In January 2024, the term was included in the outcome document of the Third South Summit held in Kampala, Uganda. For the first time, 134 member States of the Group of 77 collectively agreed to place "the Global South onto a more influential and equal footing in the international arena and in mutually beneficial cooperation with all partners" (Group of 77, 2024).

In short, although the lack of an "alternative shorthand for politicians and journalists" (Nye, 2023) was a factor behind the adoption of the global South in international policy vernacular, its mainstreaming over the past two decades reflects an element of the shared identity, economic potential and common challenges of developing countries.

The current inflection point in global economic integration is testing the countries of the global South individually and as a group. To understand why, the next section explores the main policy lessons from the first period of the rise of the global South.

In 2024, the Group of 77 collectively agreed to place the global South onto a more influential and equal footing in the international arena.

[28] General Assembly resolution 1710 (XVI) on the first development decade.
[29] General Assembly resolution 1995 (XIX) on establishing UNCTAD and General Assembly resolution 3201 (S-VI) on the new international economic order.

2. The myth of decoupling

At the start of the 2007–2009 global financial crisis, growth in the global South was widely thought to have "decoupled" from the crisis-ridden North.

In the early 2000s, expectations of the historic rise of the economies of the global South rested on high rates of growth in China and other developing economies. These were further reinforced by the apparent resilience of the developing world to the financial crisis of 2007–2009. This resilience was so remarkable that, in the early days of the global financial crisis, growth in the South was widely expected to "decouple" from the difficulties confronting the advanced economies (Akyuz, 2012). As the advanced economies slowed under the pressures of austerity policies and indebtedness, financial resilience and strong reserve positions seemed to herald robust growth ahead for most of the developing world.

Developing economy resilience to the 2007–2009 external financial shock was seen as heralding the rise of a post-United States world.

The theory of the global South decoupling from the global North rested on several arguments. First, the very nature of the 2007–2009 crisis was quite distinct. Unlike earlier crises across the developing world in the 1980s and 1990s, the global financial crisis was a "very North Atlantic credit crunch" (Nesvetailova and Palan, 2008; Tooze, 2018) or a "First-World debt crisis" (Wade, 2008). The financial implosion centred on a segment of the mortgage market in the United States. It spilled over to banking systems in Europe and revealed, among other problems, the vast size of an unregulated shadow banking system that played a central role in the transmission of systemic risks. This new, largely unanticipated "Minsky type" crisis in highly financialized economies initially appeared to have had a disproportionate impact on advanced countries and a more limited effect on developing countries, where non-bank financial intermediation and credit interlinkages were less advanced (Whalen, 2007; Griffiths-Jones and Ocampo, 2009).

The countries of the global South not only weathered the brunt of the shock but many also, during 2010–2011, grew at or above pre-crisis rates. Having shrugged off the fallout from the global recession, they were recovering with "a healthy dose of certainty and momentum" (Abiad et al., 2012: 4). On the whole, the World Bank (2018) observed, developing economies "managed the global recession relatively well, especially those that were less dependent on external trade and finance, and those with strong pre-crisis fundamentals". To many commentators, comparative resilience to the financial shock across developing economies was an important marker of the decline of the power of the United States and the rise of a post-United States world (Zakaria, 2008).[30]

The decoupling theory would not stand the test of time, however. Crisis resilience across the global South would prove transitory. It was soon apparent that the umbrella notion of the "rising South" concealed vast differences in regional experiences of the global recession. Many developing countries had to provide rescue packages to bolster their financial systems and/or to implement expansionary monetary policy (UNCTAD, 2010).

The 2007–2009 crisis came on top of a period of highly volatile commodity prices and exchange rates, which increased uncertainty and reinforced a vicious circle of falling trade flows and investments. Food and fuel price spikes through mid-2008 put food- and oil-importing sub-Saharan African countries under severe stress, depleting foreign exchange reserves and making it difficult to pay for imports and sustain growth. While oil-exporting countries benefited from increased revenues, the boom and slump contributed to output volatility, discouraging investments in long-term productive capacity (Allen and Giovanetti, 2011).

As UNCTAD concluded at the time, the 2007–2009 crisis showed that the adoption of prudent macroeconomic policies and the accumulation of foreign currency reserves by emerging market economies "have

[30] The North is in fact more resilient to crisis, particularly in the medium and long term.

been insufficient to immunize them against the systemic risks inherent in financial globalization" (UNCTAD, 2010). The "rise" itself had been uneven and incomplete, with the commodity boom of 2003–2013 masking structural problems and vast regional divergence (UNCTAD, 2018).

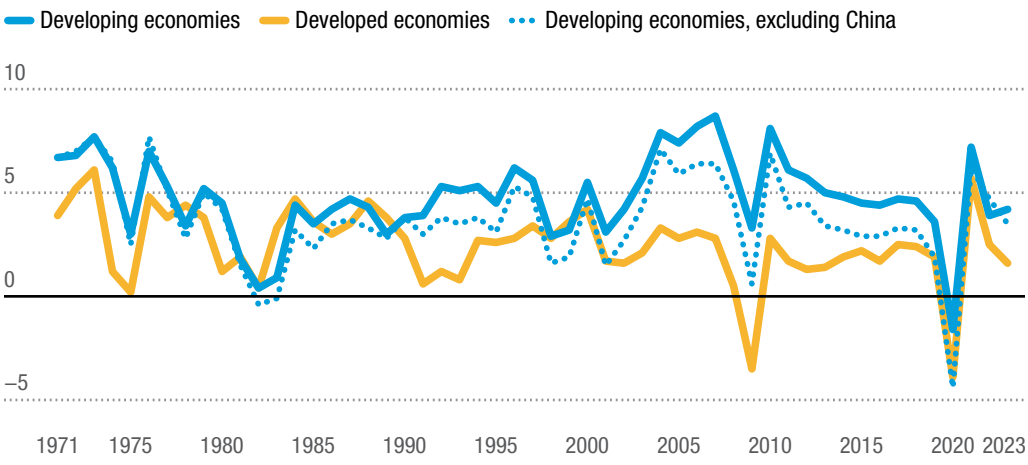
In addition, and importantly, advanced and developing countries differed in their degrees of policy space to craft a response to global uncertainty. In many developing countries, high levels of debt preceded the COVID-19 crisis. Global debt in 2019 stood at a record 233 per cent of GDP and government debt at an historic 84 per cent. The debt of developing countries totalled 180 per cent of GDP, led by private debt, which rose to 126 per cent of GDP. Four fifths of developing countries had higher debt, both domestic and external, than in 2010 (Kose et al., 2021).

Overall, the impact of the global financial crisis on the South, while not immediate, was much more severe than on the North because it fundamentally changed the growth trajectory (figure IV.3). From 2001 to 2008, the average annual growth of real GDP was about 6.7 per cent for developing countries, surpassing that of developed countries (2.3 per cent) by 4.4 percentage points. In the aftermath of the global financial crisis, from 2008 to 2019, average growth dropped for both developing countries (5.0 per cent) and developed countries (1.5 per cent), but the gap narrowed to 3.5 percentage points. After the COVID-19 shock, from 2020 to 2023, the gap fell further to 1.9 percentage points (5.1 per cent for developing countries and 3.2 per cent for developed countries).

As figure IV.3. indicates, since the global financial crisis, growth between the South and North has been gradually converging, although the South supposedly has larger growth potential. This is consistent with an earlier pattern. In the last 40 years, the five major economic crises (the 1982 debt crisis in Latin America, the 1994 Mexican peso crisis, the 1997 Asian financial crisis, the 2007–2009 global financial crisis and the 2020–2022 pandemic shock) exposed a similar trend: the South did grow faster than the North but the subsequent recession tended to be deeper in the former and it took economies there longer to recover.

Through all major economic crises of the past 40 years, the South grew faster than the North, but subsequent recessions tended to be deeper and recovery took longer.

Figure IV.3
Growth plunges across the board during crises, with the global financial crisis and COVID-19 crises having lasting effects
Real GDP growth rates
(Percentage)



Source: UNCTADstat database and table I.1.

Global growth is stabilizing at rates that are not sufficient for developing countries to address economic, social and environmental challenges.

Today's shifting global macroeconomic context adds a further alarming nuance to this general pattern. In the wake of the pandemic, global growth is stabilizing at rates that are not sufficient for developing countries to address their economic, social and environmental challenges.

3. Retreat: The divergent legacy of the 2003–2013 commodity boom

The 2003–2013 commodity boom was wide, encompassing growing demand for energy, metals and food. In a departure from earlier booms, prices for commodities behaved similarly (e.g. IMF, 2011: 47).

The 2003–2013 commodities boom revealed successful structural changes in East Asia, macroeconomic stabilization in Latin America and a lack of structural transformation in Africa.

The commodity cycle affected the three main regions of the global South differently, revealing macroeconomic, institutional and structural divergences. In Asia, strong demand for commodities led to unprecedented macroeconomic performance for most commodity exporters (OECD, 2014). In Africa and Latin America, however, the boom stalled economic diversification.[31]

The boom revealed major differences in economic transformation, namely: its success in East Asia; improved macroeconomic fundamentals in some economies in Latin America; and the absence of structural shifts in non-extractive sectors in Africa.

Asia

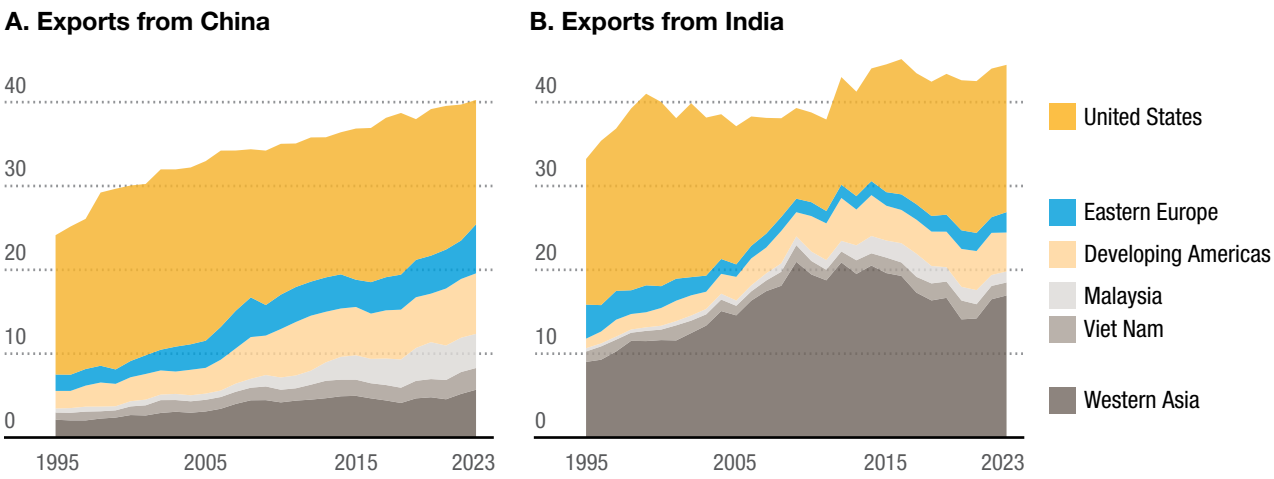
Strong demand for commodities from Asian economies was led primarily by China, which grew rapidly from 1978 to 2017 (9.5 per cent annually on average). Particularly after 2001, it provided a major boost to the 2003–2013 commodity cycle. The region became a key source of demand for commodity exports from Africa and Latin America. From 1980 to 2009, real GDP in Asian economies increased 7.5 times compared to just 3 times for the global economy. Average global income registered just under a twofold increase (Lee and Hong, 2010).

Asia's economic ascent took off due to structural factors and especially growth in capital accumulation. Although labour input, education and total factor productivity on the whole were positive, their contributions to GDP growth were more moderate (Lee and Hong, 2010). Policies of structural transformation, including the shift from agriculture to industry and services, and the continuing move within manufacturing towards higher value added products, encouraged resource shifts from low- to high-productivity sectors (IMF, 2006). From the 1990s to the 2020s, Asia became the world's processing, manufacturing and assembly hub. Its manufacturing sector value added increased from 29 to 53 per cent of global total value added from 1992 to 2021 (McKinsey Global Institute, 2023).

The second major constant in Asia's growth has been its unmatched level of regional integration, which has progressed steadily over the past 15 years (ADB, 2023a: xvi). As the COVID-19 shock challenged logistics, supply chains and labour availability, levels of consumption and investment decreased (ADB, 2023b). Yet even during the pandemic and despite trade tensions, aggregate trade held up. The severe contraction in global value chains in 2020 was followed by a rapid rebound in 2021. Figure IV.4 illustrates the dynamics of export structures for the two largest economies in the region, China and India.

[31] Asia's share in world gross product grew 20 percentage points in the last 50 years, while the shares of Latin America and Africa remained largely unchanged, at around 5 per cent. This indicates that, while the global South as a whole is catching up with the global North, not all global South regions participate in the same way (Fernandez et al., 2022).

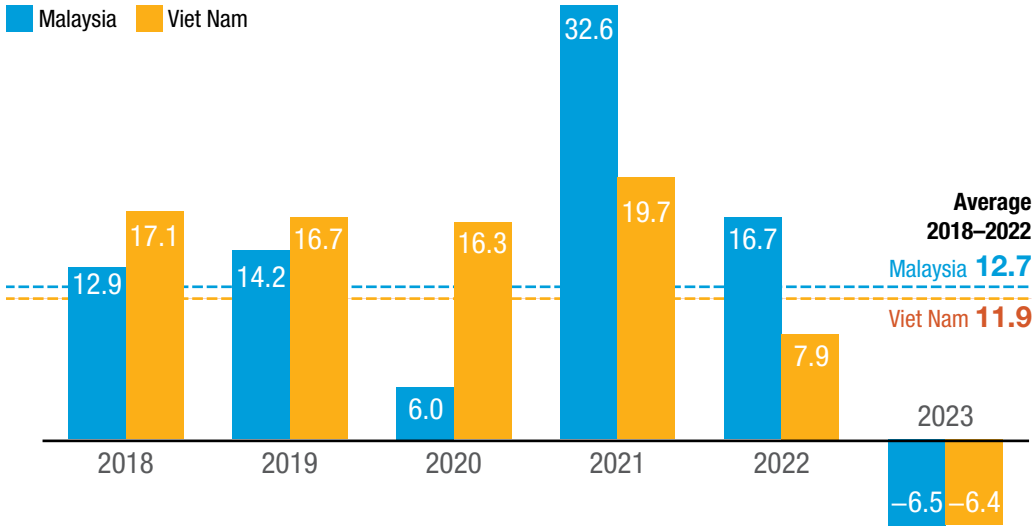
Figure IV.4
Exports have grown and held firm even during crises in the region's two powerhouse economies
Exports to selected regions
(Percentage)



Source: UNCTADstat database.

Intraregional trade helped sustain the resilience of economies in Asia during the pandemic. For instance, from 2018 to 2022, trade between China and Viet Nam grew by 12 per cent annually, and between China and Malaysia by almost 13 per cent (figure IV.5).

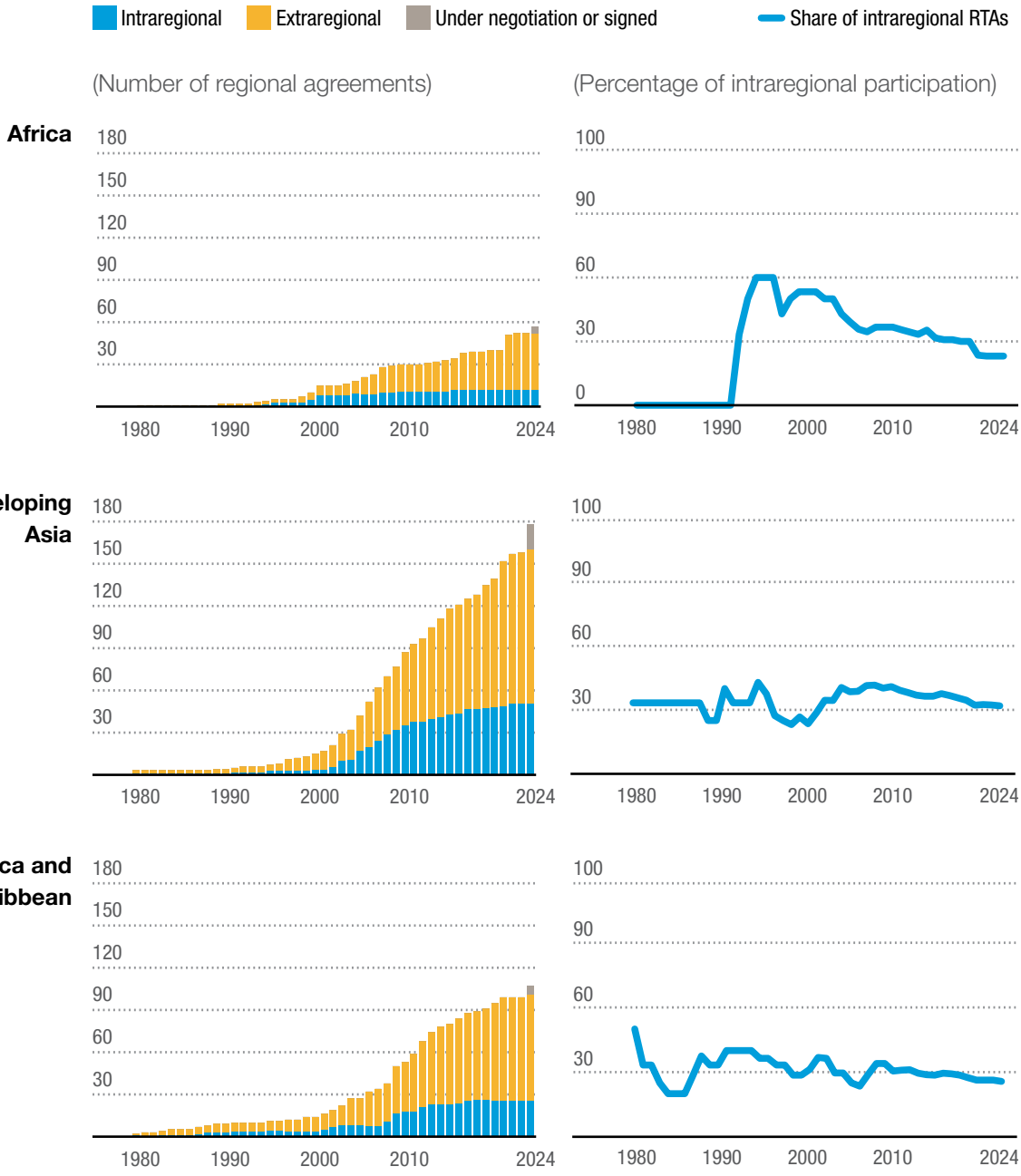
Figure IV.5
Expanding intraregional trade bolstered resilience during the pandemic
Growth rates of China's trade with Malaysia and Viet Nam
(Percentage)



Source: UNCTADstat database.

Trade integration is a continued strength of Asian economies insofar as regional trade agreements have the potential to mitigate supply chain disruptions (ADB, 2023a: 10). Figure IV.6 shows that the participation of developing Asian economies in intraregional trade agreements has grown progressively since the early 2000s and is substantially above rates in Africa and Latin America.

Figure IV.6
Countries in Asia participate in more regional trade agreements, smoothing disruptions when supply chains falter
Regional trade agreements in force



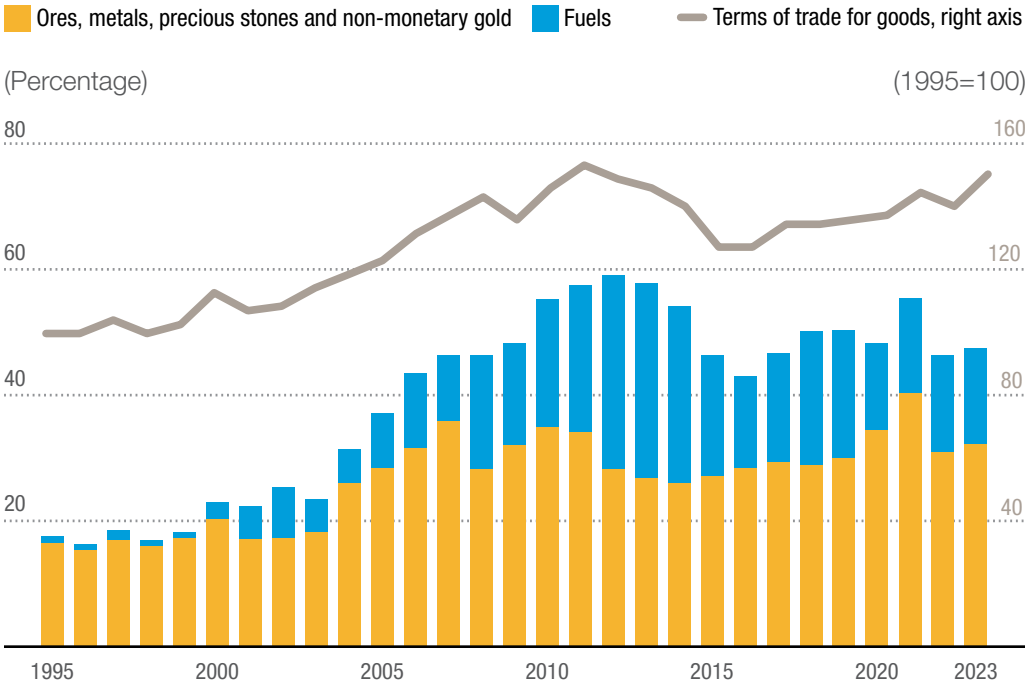
Source: UNCTAD based on World Trade Organization, Regional Trade Agreements, 2024.

Notes: RTAs, regional trade agreements. The share of intraregional RTAs in total (intra plus extra) RTAs is based on RTAs in force where all parties are from the respective region.

Latin America

Countries in Latin America benefited considerably from greater demand in Asia for natural resources from 2003 to 2013. Terms of trade for commodity exporters peaked in April 2011, when metal prices started to fall. Figure IV.7 shows that the situation reversed in June 2014 with an oil price shock that hit oil and natural gas exporters the most, namely, the Plurinational State of Bolivia, Colombia and Ecuador. Commodity terms of trade remained broadly unchanged from 2014 to 2019 for metal exporters such as Chile and Peru, after falling from 2011 to 2014 (Balakrishran et al., 2021: 5).

Figure IV.7
Demand for natural resources in Asia has boosted exports from Latin America but with variation over time and by commodity
Share of selected commodity groups in total merchandise exports from Latin America to developing Asia

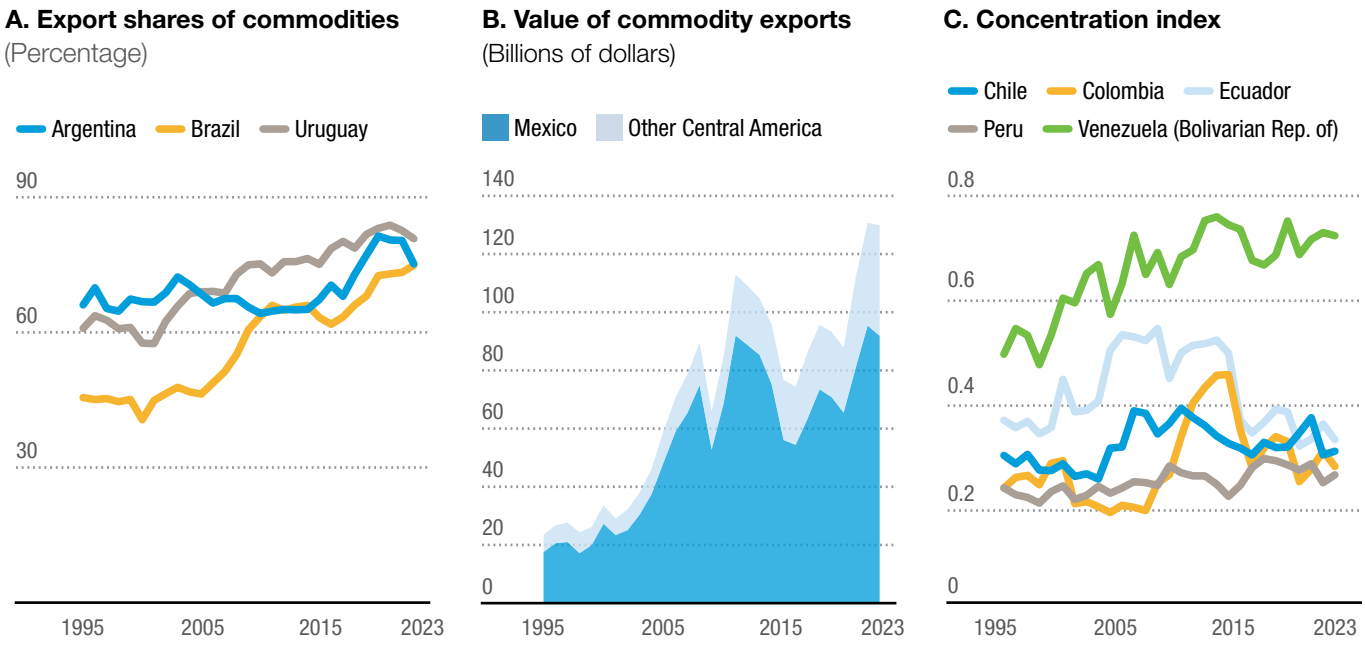


Source: UNCTADstat database and Cepalstat database.

Across Latin America, despite some diversification away from commodities, the commodity boom still saw primary goods accounting for 60 per cent of total exports on average (figure IV.8). Argentina, Brazil and Uruguay experienced a significant increase of their export shares of commodities. Heavy metal or energy exporters such as Chile, Colombia, Ecuador, Peru and Venezuela did not embrace significant diversification and were, consequently, more vulnerable when the cycle reversed. In Mexico and Central America, commodity exports fell by half between 1970–1980 and 2010 (IMF 2011: 51). These differences notwithstanding, during the boom, the reliance on commodities in Latin America appeared broadly unchanged since the 1970s (IMF 2011: 62).

Figure IV.8
In Latin America, diversification away from commodities has been limited

Primary commodity exports and concentration index, selected countries



Source: UNCTADstat database.

Notes: The product concentration index shows to which degree exports and imports of individual economies are concentrated on a few products rather than being distributed in a more homogeneous manner among several products. It does not include services. The index value is from 0 to 1 (close to 1 means less diversified exports).

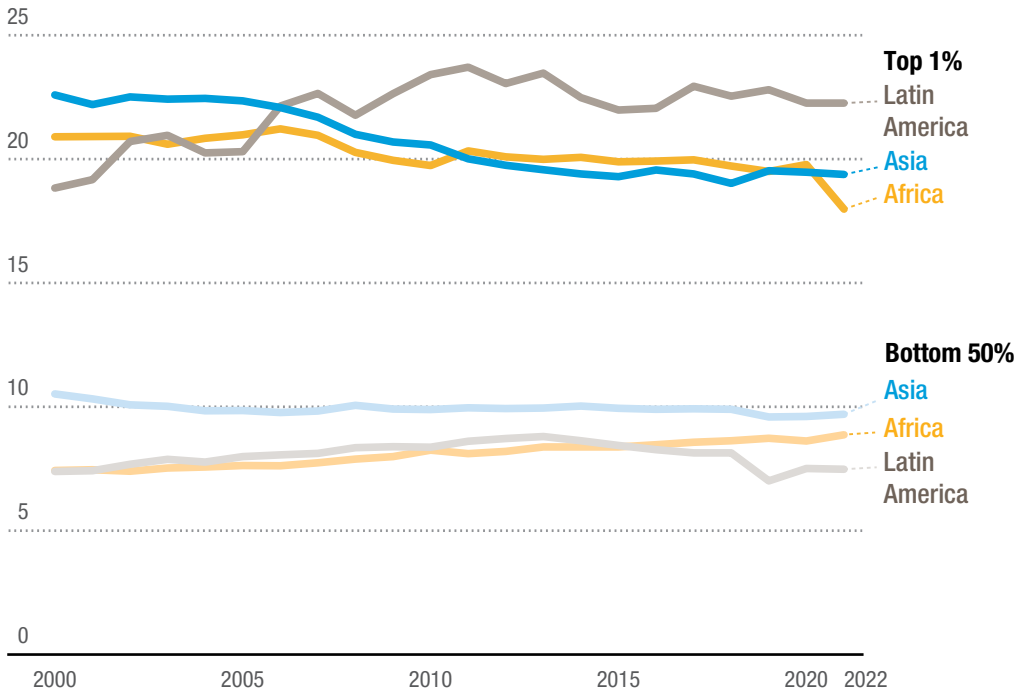
Renewed growth in the share of natural resource goods in the export basket of Latin America, described as "reprimarization" or "recommoditization", accentuated the region's high natural resource dependence (OECD, 2014; Ocampo, 2017). In exports from Latin America to China, which became the region's major trading partner, commodities represented over 90 per cent of the total. Booming Chinese imports contributed to reprimarization by weakening the manufacturing sectors in several Latin American countries (Ocampo, 2017).

The commodities boom enabled progress in reducing poverty and inequality. Both Central and particularly South America recorded diminishing inequality rates. From 2000 until the onset of the pandemic in early 2020, measures of multidimensional poverty fell in every country in Latin America (UNDP, 2021).[32] Yet in many commodity exporters, poverty reduction came to a halt between 2013–2014 (the end of the commodity boom) and 2020 (the onset of the pandemic) as labour markets stagnated and real wages decreased (Balakrishran et al., 2021). Poverty increased in a few cases, as in Argentina and Brazil, yet on average, the impressive gains of the boom did not so much reverse as stagnate (Balakrishnan et al., 2021). Compared to other region of the global South, income inequality remains high in Latin America (figure IV.9).

[32] Multidimensional poverty measures include: nutrition, child mortality, years of schooling, school attendance, cooking fuel, electricity, drinking water, sanitation, housing and assets (UNDP, 2021).

Reduced inequality and particularly poverty during the commodities boom stemmed from increased fiscal spending and labour demand in low-skill sectors, such as construction and services, that were directly tied to resource production (Balakrishran et al., 2021). Political will to increase social spending on innovations such as non-contributory programmes for the poor also contributed to positive outcomes (Sánchez-Anchochea, 2021; Gasparini and Cruces, 2021).

Figure IV.9
Income inequality remains high, particularly in Latin America
Pre-tax national income shares of the top 1 and bottom 50 percentiles, by region
(Percentage)



Source: World Inequality Database.

Note: Asia includes developing and developed countries.

In the region as a whole, declining inequality resulted from better short-term government management of the commodity boom relative to previous episodes. Labour market formalization and improved minimum wages were promoted along with measures to "control a higher share of commodity rents than in the past" (Sánchez-Ancochea, 2021) and to reduce tax avoidance (Gasparini and Cruces, 2021). Yet generally, Latin America still has significantly higher income inequality than its degree of development would suggest, and it remains the most unequal region in the world (Galindo and Izquierdo, 2024; Gasparini and Cruces, 2021).

In stark contrast to Asia, the participation of countries in Latin America and the Caribbean in global value chains has lagged. Uneven trade policies in the region, the fragmented nature of interregional trade, and the lack of common preferences and rules of origin in the network of preferential trade areas have all hampered the development

of supply chains (Moreira and Stein, 2019: 50–51). According to the Inter-American Development Bank, "although there is growing evidence that the fragmentation of global trade could benefit some Latin American economies, in the current context, the leading indicator for the region's exports does not point to a change in the trend in the first half of 2024" (IDB, 2024: 10).[33]

Africa

In the early 2000s, the notion of "Africa rising" and even "lions on the move"[34] embodied many assumptions about the rise of the global South more generally. Africa holds some 12 per cent of the world's oil reserves, 42 per cent of its gold, 80 to 90 per cent of chromium and platinum metals, 60 per cent of arable land and large timber reserves (African Union, 2021). Commodities account for more than 60 per cent of exports in 46 of the continent's 54 countries (UNCTAD, 2022a).

Yet for this resource-rich continent, a "rise" would prove to be short-lived, closely mirroring the 2003–2013 commodity cycle. From 2004 to 2014, the continent experienced an unprecedented boom in mineral production and prices driven by high demand in Asia's industrializing economies. This was particularly the case for the oil and gas sector. Africa's top 10 producers generated an extraordinary $2.3 trillion in revenues from 2004 to 2014 (International Energy Agency, 2019).

In addition to major producers such as Angola and Nigeria, and a number of longstanding medium-scale producers (Gabon and the Republic of the Congo), a large number of countries saw corporate interest in their oil and gas potential and eventually became hydrocarbon exporters (Oppong and de Oliveira, 2021).

Among them, Mozambique loomed large, having seen the discovery of some of the world's largest natural gas reserves in 2010 (Salimo et al., 2021). Foreign direct investment in extractive industries began coming not just from the western oil and mining corporations that dominated the continent until 2000 but also from a large number of companies from the global South, especially China and India.

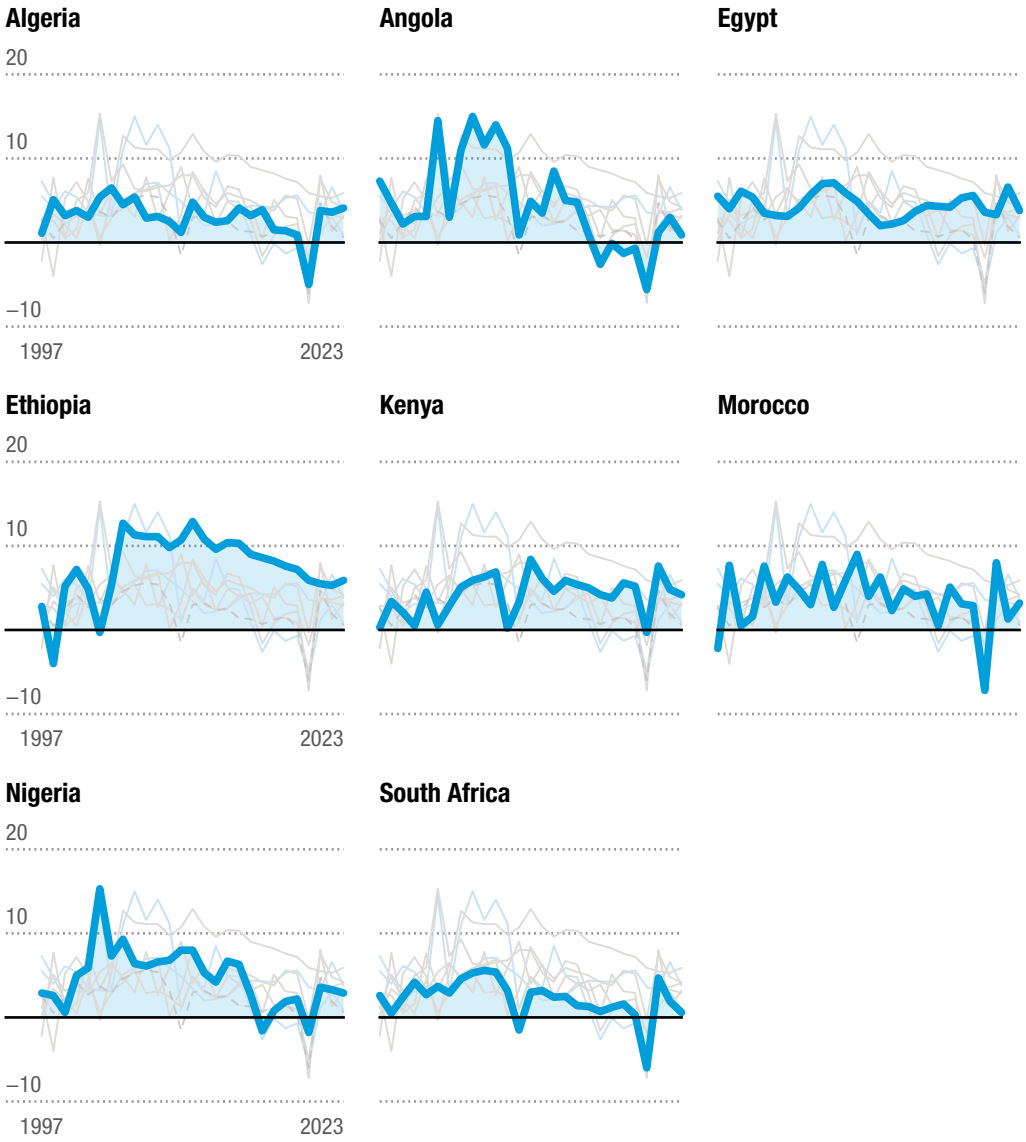
Overall, from 2000 to 2010, Africa grew by an average of 5.1 per cent per year, but the rate slowed to 3.3 per cent in 2010–2019 (Tran, 2024). Sub-Saharan Africa's GDP per capita peaked in 2014 at $1,936 and has since fallen more than 10 per cent to about $1,700 in 2023. In the same period, global GDP per capita rose nearly 15 per cent (Blas, 2023). Commodity exporters in Africa have seen low growth since 2014, and the largest economies on the continent (such as Angola, Nigeria and South Africa, all commodity exporters) have had particularly disappointing trajectories (figure IV.10).

[33] Mesquita et al. (2022) find some evidence that "near-shore" suppliers such as Mexico gained ground, particularly after the 2008 crisis. These gains seem to have come at the expense of producers in the United States, however, instead of "far-shore" suppliers in Asia, which continued to strengthen their position. This point is challenged by Utar, Torres Ruiz and Zurita (2023). Looking at firm-level data in Mexico from 2015 to 2021, they find that the "U[nited] S[tates]–China trade war had a significant impact on [Mexican] firms' exports… Mexico's GVCs in manufacturing and services are a substitute for China's GVCs and complements U[nited] S[tates] manufacturing. In particular, Chinese import protection in the U[nited] S[tates] over 2018–19 has a significant positive impact on Mexican GVC firms' exports to the U[nited] S[tates], amounting to a 16.5 [per cent] increase in 2019". They add that "despite a temporary dampening of this effect in 2020 at the height of the COVID pandemic, the positive effect remains significant at 17 [per cent] by 2021. The protectionist turn in the U[nited] S[tates] targeting China also causes imports of Mexican GVC firms from the U[nited] S[tates] and Asian countries to increase, but less so than their exports, resulting in a significant increase in their overall net exports". Hence, they conclude that "the recent shift in U[nited] S[tates] trade policy played a role in reshaping GVCs and provide evidence of their relocation towards Mexico" (Utar, Torres Ruiz and Zurita 2023: 3).

[34] See especially McKinsey, 2010 and Radelet, 2010.

Figure IV.10
A downward trend is evident in major African economies dependent on commodities

Real GDP growth rates in the largest African economies
(Percentage)



Source: UNCTADstat and table I.1.

The continent has not fully recovered from the pandemic, having lost 2.4 percentage points of GDP relative to the pre-COVID-19 trend as of 2023. Its income gap with the rest of the world has widened, to its disadvantage (Tran, 2024). One hypothetical projection gives an idea of the scale of the gap between Africa and the advanced economies today. UNCTAD calculations suggest that the 55 countries of the African Union would need to grow by 19 per cent per year for the next 20 years simply to reach Group of Seven living standards today.

At the same time, it is important not to overlook the legacy of benefits of

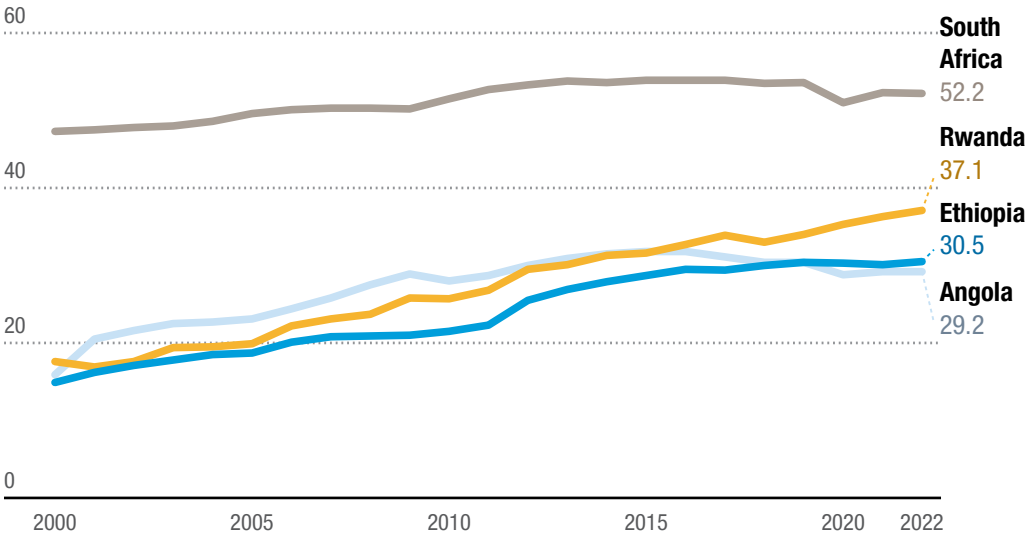
the commodity boom. The era of high commodity prices was a welcome respite from previous decades of economic decline. It enabled economies to return to strong growth, address late twentieth century debt burdens and shake off the most stringent forms of structural adjustment mandated by the international financial institutions. Amid increased foreign direct investment and the strong diversification of investors, particularly Asian industrializing economies, prospects for a qualitative improvement seemed promising.

Economic improvements in the early 2000s enabled African States to emphasize the role of public institutions in fostering national development (Péclard et al., 2020). Resource-rich States such as Angola, which experienced an oil boom after the end of the civil war in 2002, pursued capital-intensive industrial projects. Even resource-poor countries, such as Ethiopia and Rwanda, sought to implement ambitious diversification policies. Despite limited financial means, these two countries arguably have a better record of economic diversification over the last two decades, albeit starting from very modest baselines (figure IV.11). Elsewhere on the continent, the results of diversification have been disappointing.

Slow or absent structural transformation adds to a more pessimistic picture. Between 1980 and 2000, the modest manufacturing share in African GDP fell by half (Jacquemot, 2018). In sub-Saharan Africa, despite interest from potential investors, manufacturing declined from 18 per cent of GDP in 1981 to 11 per cent in 2023 (Pilling, 2024).

In essence, the period from 2000 into the 2010s was a period of jobless growth. Expectations of the continent's many young people remained unmet. Africa creates about 3 million formal wage jobs a year, but 12 million young people will enter the labour force every year over the next decade. The continent suffers from high unemployment among people aged 15–24, averaging more than 20 per cent. South Africa has

Figure IV.11
Diversification, even from a low baseline, helped Ethiopia and Rwanda boost productive capacity
Productive capacity index, selected African countries



Source: UNCTADstat database.

Note: For details on the productive capacity index, see note for figure III.13.

the highest youth unemployment rate in the world, at 61 per cent (Tran, 2024).

Enthusiasm about the consumer potential of an African rising middle class is now considered exaggerated, as is the size and geographic distribution of this class (e.g. Melber, 2017). Poverty alleviation has not progressed in much of the continent, and absolute numbers of poor people continue to increase. While there are some clusters of Asian foreign direct investment in African manufacturing, the "flying geese" theory of industrialization has not borne fruit. In terms of the absolute size of manufacturing value as well as an increase in manufacturing jobs, the continent has continued to industrialize (Abreha et al., 2021). Yet there has been industrial decline in Africa's hitherto most industrialized economy, South Africa. African economies in general have found it very difficult to insert themselves in global value chains (Abreha et al., 2021).

International financial integration has come at the cost of higher debt burdens for many countries. By 2018, 10 of 13 countries that had acquired a high risk of debt distress since 2013 were in sub-Saharan Africa. From 2017 to 2023, 46 of the 57 developing countries, or 81 per cent, experienced a deterioration in external financial sustainability, with a median annual increase in debt service costs of 16.3 per cent, far outstripping growth in exports plus remittances of 5 per cent. Twenty-seven countries with deteriorating positions were in Africa, 14 were in Asia and 5 were in Latin America and the Caribbean (UNCTAD, 2024b). In 2023, among the 25 countries with the highest proportion of export earnings allocated to total external debt servicing, 9 countries were from Africa (figure IV.12).

From the vantage point of the post-boom years, the vast majority of African economies clearly saw little structural transformation towards non-extractive sectors. In 2024, African economies are outliers compared to industrial economies and other developing economies. They retain a strong natural resource focus, a very low degree of integration in global value chains, mostly poorly educated labour forces and few prospects of competing with agile global South peers, whether in manufacturing or commercial agriculture.

4. Summary

In retrospect, therefore, the 2003–2013 rise of the global South has been both uneven and incomplete. Asia's advance towards becoming a global economic centre was an outcome of structural transformation domestically and increased economic integration regionally.

In Latin America, growth during the first two decades of the new century was based on conjunctural factors, such as the commodity boom, although macroeconomic policy and financial regulation proved effective and consistent with the goals of inflation control and financial stability. Notable exceptions were Argentina and the Bolivarian Republic of Venezuela.

Africa, despite successful diversification away from non-extractive sectors in several countries, such as Ethiopia and Rwanda, has gone through a commodity-driven boom of jobless growth. Despite a significant emphasis on industrial policy, most resource-rich economies were just as dependent on natural resources in 2013–2014 as they had been before. Today, the continent remains heavily dependent on its resource base, while a heavy financial legacy of debt burdens exacerbates long-term problems of poverty, insufficient structural reforms and anaemic development overall.

Figure IV.12
Top 25 developing countries with highest amount of export earnings spent on debt servicing

Debt servicing as a share of export revenues
(Percentage)

Emerging market economies
2022 2012

Frontier market economies
2022 2012

Other developing economies
2022 2012

Source: UNCTAD based on World Bank International Debt Statistics and the IMF *World Economic Outlook* (April 2024).

C. Repositioning: New pathways to development

The regional diversity of the global South raises important questions about the direction and type of development strategies at an inflection point for globalization.

Geoeconomic changes cast doubts about some previously prevalent assumptions, such as the notion that East Asian industrialization can be emulated elsewhere in the global South today. Several issues put such ideas into question.

First, East Asian integration closely resembles traditional trade and investment relations between the North and South. Yet a "flying geese" model of industrialization and regional integration has not borne fruit in Africa or Latin America. Expectations that the "flying geese" typology provides a realistic depiction of East Asian industrialization and its potential implementation across the global South tend to gloss over the typology's analytical shortcomings and inevitable reductionism. They exaggerate its policy relevance (Saad-Filho, 2014), as critiques of the Asian model have suggested (e.g. Das, 2015).

Second, the current diversity of the global South is reflected in the interrupted trajectories of some regional economic leaders. In the 1990s, for instance, Chile was hailed for its closeness to the East Asian model (Paik et al., 2011). Today, the country's inadequate tax collection imperils public services; bureaucracy slows investment; and the manufacturing sector remains small compared with emerging world peers, including neighbouring Argentina. Mining products such as copper account for most exports and billionaire wealth, making Chile look more like an old-fashioned commodity economy than an East Asian tiger (Sharma, 2024).

In South Africa, the largest economy in Africa, the implosion of the 2003–2013 commodity boom exposed the country's many fault lines, including youth unemployment above 50 per cent, a high share of the population on welfare, weak investment and recurrent power outages. Even in Asia, Thailand, one of the original "Asian Tigers", has seen its per capita GDP decline. It has one of the world's highest inequality rates, with 79 per cent of the poor living in rural areas. Despite efforts to become a factory hub based on its location on global trade routes, productivity is stagnating, and Thailand is losing out to manufacturing rivals such as Viet Nam (Sharma, 2024).

Today, the assumption that East Asian industrialization can be successfully emulated as a development model elsewhere in the global South is in doubt.

Third and finally, new constraints on prospects for Asian-style development and industrialization arise from the impact of the new growth wave discussed in chapter III. The development successes of the 1990s, regionally and nationally, may not be easily emulated amid a new commodity cycle, the energy and technology transition, advanced financialization and the shift towards services as the dominant sector of the economy.

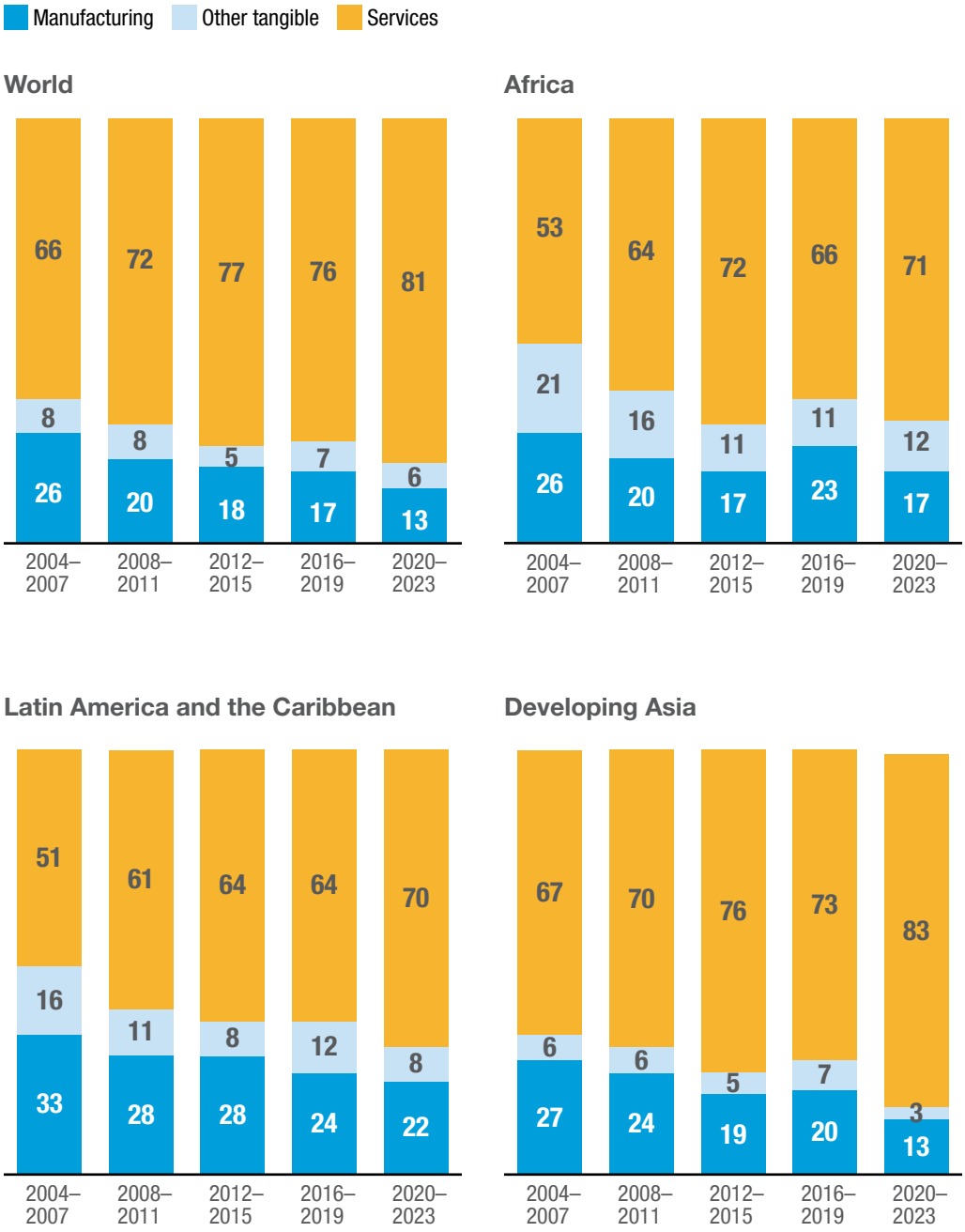
The geography of service-oriented foreign direct investment reflects the current diversity of the global South (figure IV.13), where developing Asia continues to account for the bulk of the increase in greenfield investment flows. While shares of service-oriented investment projects in Africa and Latin America rose from 2020 to 2023, overall investment has stagnated since 2020. At the same time, the growing importance of service industries and intangible assets in global value chains can pose risks to developing economies as a whole. This may exacerbate existing structural barriers holding back the world's least developed countries and could magnify their vulnerability to external shocks (UNCTAD, 2018).

Developmental success stories of the 1990s may not be easily emulated amid the new commodity cycle, energy and technology transition, advanced financialization and servitization of the economy.

Figure IV.13
Changing investment flows favouring services may worsen structural barriers

Structure of foreign direct investment, by region and sector
(Percentage of total number of cross-border greenfield projects)

A. By region



B. By Sector

	2004–2007	2008–2011	2012–2015	2016–2019	2020–2023
Manufacturing					
Africa	3	5	5	6	5
Latin America and the Caribbean	8	11	14	13	13
Developing Asia	37	40	34	31	27
Rest of the world	51	44	47	50	55
Other tangible					
Africa	9	10	12	8	8
Latin America and the Caribbean	12	12	15	16	11
Developing Asia	26	27	33	27	14
Rest of the world	52	51	40	50	67
Services					
Africa	3	5	5	4	4
Latin America and the Caribbean	5	7	7	7	7
Developing Asia	36	34	31	26	27
Rest of the world	57	55	57	63	63
Total					
Africa	3	5	5	5	4
Latin America and the Caribbean	6	8	9	9	8
Developing Asia	36	34	31	27	26
Rest of the world	55	52	54	60	62

Source: UNCTAD based on information from the *Financial Times* FDI Markets database.

Notes: The sectoral analysis is based on the variable "Business activity". Crucially, this means that "Services" include services activities within typical manufacturing industries (for example, sales offices of car manufacturers). "Manufacturing" is as classified in the database. "Other non-services" includes several activities normally classified as services but physical asset-heavy in nature; it comprises the following categories: construction, electricity, extraction and infrastructure. "Services" includes all remaining (service-related) business activities. The business activity "ICT and Internet infrastructure" was split into Internet infrastructure, allocated to "Other non-services", and the remaining part of ICT services allocated to "Services".

Finding new pathways to successful development requires re-evaluating the commodity cycle and devising policies to achieve diversification and redistribution.

Within this changing context, new pathways to successful development and sustainable growth can still be found. For many countries in the global South, this requires re-evaluating the short-term benefits of the commodity cycle as well as rising shares of services and finance-related sectors. New policies are needed aimed at long-term diversification and redistribution.

The continued influence of financialization – denoting the growing role of financial instruments, activities and valuations (Sawyer, 2013) – across the real economy, trade and global value chains, carries major implications for developing countries pursuing economic integration. Some are examined below.

Across the real economy, trade and global value chains, financialization has major implications for integration strategies.

1. The challenges of financialization, old and new

Given lessons from the 2003–2013 commodity boom as well as a new wave of growth and the energy transition, careful management of the expansion of extractive industries is increasingly important for many resource-exporting countries of the global South. In 2018, 18 out of 27 surveyed developing economies experienced increased shares of extractive industries in export value added. Some registered spikes topped 10 percentage points (UNCTAD, 2018).

For many developing countries, commodity booms are closely intertwined with the financial cycle and associated risks of financialization. The financialization of commodity markets and industries has progressed since 2000, when the deregulation of derivatives markets in the United States and a wave of new financial innovations incentivized banks, hedge funds and other types of investors to trade and speculate on commodity-based index products. Many institutional investors were attracted to commodity-based products by the prominent narrative that a growing population would generate ever-growing demand for the world's natural resources, and that food production would need to grow by 50 per cent or more in the coming decades (FAO, 2017; Clapp, 2019).

A more recent development is the energy transition. With its mounting demand for commodities, especially minerals, it is unfolding under the influence of advanced financializaton (e.g. Knuth, 2018; Appiah et al., 2023). Managing the expansion and financialization of extractive industries constitutes a key challenge for commodity exporters as the energy transition and new growth wave move forward.

Extractive commodity industries, namely, mining and energy, are extremely capital-intensive; rents tend to be concentrated in the hands of the owners of capital. In agricultural commodity sectors, activities are labour-intensive. The majority of producers in developing countries are small in scale and only participate in the lower value added segments of international food chains, retaining a fraction of the value added of what they produce. Coffee producers, for example, earn as little as three per cent of the final price (UNCTAD, 2018).

Against growing control of the agriculture sector by a few multinational enterprises, smallholder producers face the combined challenges of high cost and limited access to inputs; inadequate capital; growing requirements to comply with safety, quality and environmental standards enacted by importing countries; and increasing weather variability with limited tools for adaptation (UNCTAD, 2024a).

Conversely, during recent years of market turbulence, the profits of commodity trading giants that control, conservatively, up to 70 per cent of global food markets have soared, in many cases boosted by financial speculation (UNCTAD, 2023). For instance, the global grain trade is dominated by a small number of firms in highly financialized commodity markets prone to volatility (Clapp, 2022). The speculative practices of these companies

have been a policy concern even as the lack of regulatory attention and corporate arbitrage enable them to profiteer in periods of crisis and market volatility (UNCTAD, 2023; Clapp, 2022).

Definitions of financialization vary across academic disciplines (van der Zwan, 2014), but the phenomenon can be understood both as the greater tradability of underlying assets in financial markets and the predominance of profits from financial ventures over revenues from core business activities. Balancing the exposure of commodity-exporting countries to financialization externally while regulating the growth of extractive industries within the domestic macroeconomy constitutes a twofold challenge for policymakers in many developing countries. This is for several reasons.

First, in developing countries, the relationship between financial cycles and commodity prices tends to be particularly pronounced (Aldasoro et al., 2023). The precise role of commodity markets in the transmission of the financial cycle to developing countries remains debated, but recent research suggests that the endogenous response of export prices plays a major role in amplifying the transmission of monetary policy in the United States to developing countries. This is due to the sensitivity of commodity prices to interest rates, and because changes in monetary policy in the United States and global risk appetite are key drivers of capital flows in commodity-exporting economies (Juvenal and Petrella, 2024).

Figure IV.14 shows the close relationship between the financial cycle and commodity prices since the early 2000s, when the introduction of commodity-based index products in international financial markets widened opportunities for financial speculation (Gkanoutas-Leventis and Nesvetailova, 2015).

Financial cycles tend to be much slower moving than commodity price cycles, where the frequency is closer to that of capital flows. Figure IV.14 presents a correlation in line with findings by Aldaroso et al. (2023). Namely, the first principal component of capital flows to emerging markets is much more strongly corelated with commodity prices than the respective first principle component of capital flows to advanced economies.

The negative impacts of financialization on economic stability and income distribution in developing economies were documented in pre-pandemic analyses (Bonizzi, 2013; Kaltenbrunner and Painceira, 2015). Recent research (Sharma, 2022) finds that the effects of the financialization of commodities became more pronounced during COVID-19 compared to the 2008–2009 period.

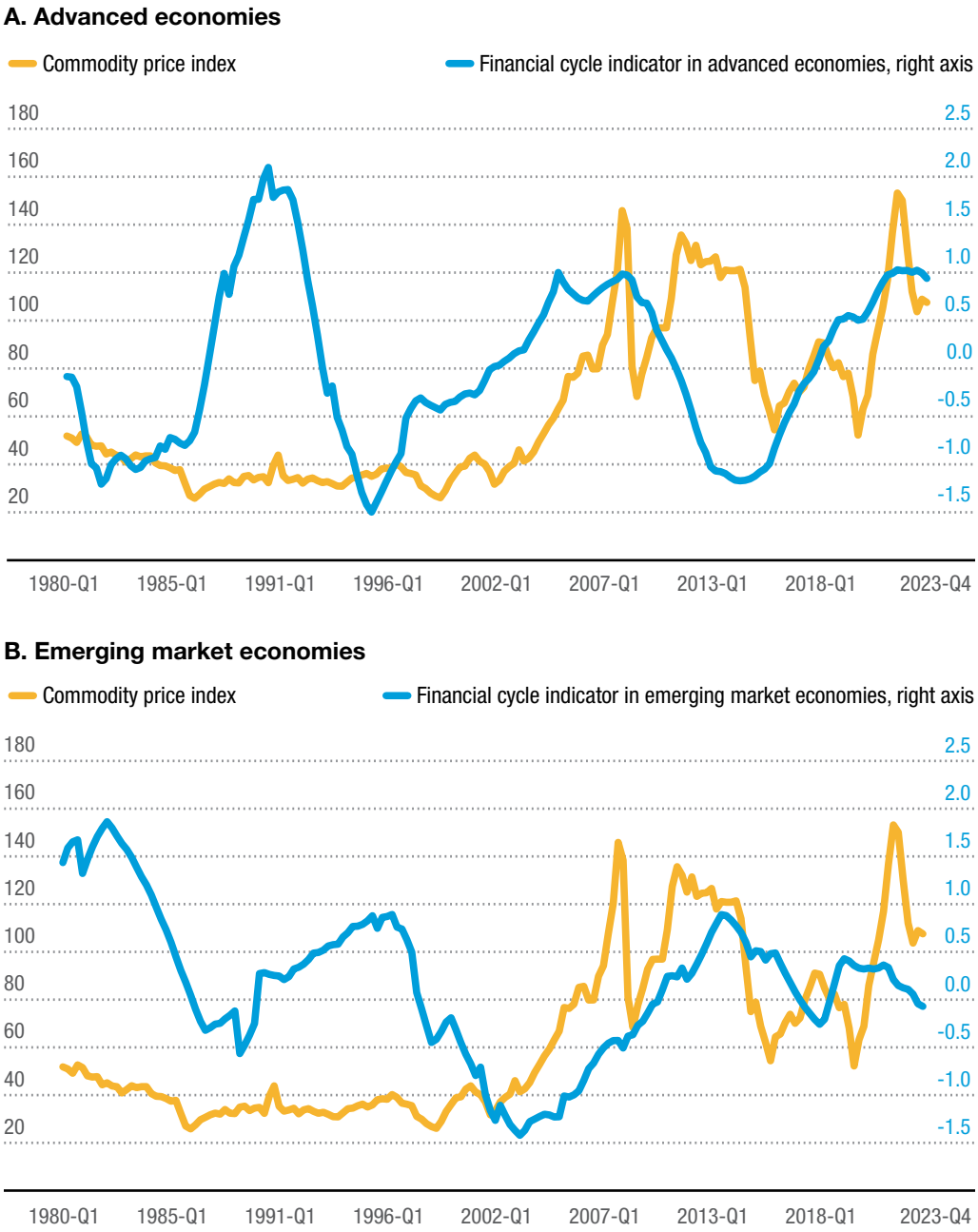
Recently this analysis was advanced by new empirical studies of the financialization of commodity value chains (box IV.1). They suggest that the financialization of commodities and the concentration of global value chains effectively constitute a twofold problem for exporters in the global South. In part, this is due to the fact that although at the aggregate level financial institutions and markets play a central mediating role, financial investments on the ground, at different stages of value chains, are mediated through asset management firms and corporate practices.

Financialization entails the greater tradability of underlying assets and the predominance of profits from financial activities over revenues from core business activities.

In developing countries, the relationship between financial cycles and commodity prices tends to be pronounced.

The effects of the financialization of commodities became more pronounced during COVID-19 compared to the 2008–2009 period.

Figure IV.14
Is a commodity cycle a financial cycle? Evidence shows a close relationship, more so for emerging markets
Financial cycle indicator and commodity price index (2010=100)



Source: UNCTAD based on Fitch; national data; Bank for International Settlements; World Bank commodity price data.

Notes: Q1, first quarter; Q4, fourth quarter. Financial cycles are measured by frequency-based (bandpass) filters capturing medium-term cycles in real credit, the credit-to-GDP ratio and real house prices (Borio, 2014). Financial cycles are normalized by country-specific means and standard deviations before simple averages are taken for country groupings. Emerging market economies comprise: Brazil, Chile, China, Hong Kong (China), Colombia, Czechia, Hungary, India, Indonesia, Israel, Republic of Korea, Mexico, Malaysia, Singapore, South Africa, Thailand and Türkiye. Advanced economies comprise: Australia, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, the Kingdom of the Netherlands, Norway, New Zealand, Portugal, Spain, Sweden, Switzerland, the United Kingdom and the United States.

Box IV.1
Ghana: The peculiar case of a cocoa pricing mechanism

The price of cocoa beans is highly volatile and largely determined at international commodity exchanges in London and New York. In Ghana, the economy relies heavily on cocoa bean exports to generate foreign reserves. Volatile cocoa prices, however, translate into swings in revenues, income and exchange rates, posing risks to internal and external balances.

Ghana is the only country that has maintained a State monopoly on cocoa bean sales. The Cocoa Marketing Company, a subsidiary of the Ghana Cocoa Board or Cocobod, manages the monopoly and is registered as a limited company.

In the early 2000s, Cocobod introduced a system enabling the national Bank of Ghana to access international money markets for cheap credit. This entails a loan offered by a group of lenders and collateralized with forward contracts to buy or sell cocoa at a specified price in the future (van Huellen and Abubakar, 2021). Originally, the system was designed to finance foreign exchange requirements to import oil. To date, this arrangement, called a syndicated loan, has provided the Bank of Ghana with its main access to international money markets.

More than 80 per cent of the price received by the Cocoa Marketing Company is derived from the international market based on contracts for future sales and purchases over which the company has no control. Since pricing is forward-looking and speculative, it reflects traders' expectations about future demand and supply conditions, which are subject to volatile market swings and changes in investor sentiment.

The ability of the Cocoa Marketing Company to time price fluctuations in the market is curtailed by financing requirements for internal marketing. The syndicated loan has to be in place by September for the company to pay farmers during the harvest. It needs to commit an appropriate volume of cocoa through forward contracts, which means locking in prices even in a rising market. This situation is well known to buyers, who use it to their advantage. The COVID-19 period demonstrated this, as buyers refused to sign forward contracts unless the Cocoa Marketing Company agreed to a negative country premium. A lack of contracts would have left the company with no money to pay cocoa farmers, which ultimately forced it to agree.

The forward-selling system allows the Cocoa Marketing Company to protect cocoa farmers against downside price risks by locking in sales prices in a declining market, but then the company loses the flexibility to benefit from rising prices. Some flexibility is maintained by reserving a portion of the harvest for spot sales. Yet the company can still be caught out by a low harvest. In times of economic turmoil and external debt crises, Cocobod and the Cocoa Marketing Company can face additional pressure from the Government to forward sell a higher volume of beans than would have been desirable given market conditions.

The Bank of Ghana gains direct access to around $2 billion annually through cocoa bean sales, which makes Cocobod one of the most important government institutions in the country. A lack of independence, however, has threatened the credibility of the Cocoa Marketing Company. After Ghana lost access to international capital markets as a result of a debt crisis and saw a higher risk premium, the syndicated loan became the sole means of accessing international markets, the biggest source of foreign exchange and the largest contributor to foreign exchange reserves.

Box IV.1 Ghana: The peculiar case of a cocoa pricing mechanism

The current system, with prices referenced to the terminal market price in London as well as multiple currency conversions, leaves the Cocoa Marketing Company exposed to significant price and quantity risk. Adjusting the existing arrangement is challenging, because it provides Cocobod with liquidity to finance its position as the monopoly buyer of Ghanaian cocoa beans. It also provides the Bank of Ghana with access to the international market at affordable rates, which is vital amid the domestic debt crisis and a continuously depreciating currency.

Calls to abolish the 30-year-old system have grown in recent years, however, prompting speculation that it is time for Cocobod to design a five-year plan to wean itself off the syndicated loan. This would reduce interest payments and allow dollar revenues from cocoa exports to continuously enter the Bank of Ghana. Funding demands persist, however, and the current IMF restrictions on the country's ability to extend funding means negotiations are required before a strategy is implemented.

Source: van Huellen et al., 2024.

2. Finance as a fresh dimension of the resource curse

Frequent and increasingly violent gyrations in international commodity prices have a direct impact on both export and fiscal revenues, foreign direct investment and exchange rates, generating macroeconomic instability. This often impedes long-term investment and revenue mobilization to achieve sustainable growth and development (UNCTAD, 2018).

Further, unregulated expansion of the financial sector may expose countries to risks of unbalanced growth, based on the contribution of the finance, insurance and real estate (FIRE) sector to overall output, value added and employment. The nature of the sector's contribution to output and value added has gained policy and research interest in the wake of the global financial crisis, although mainly in terms of advanced economies with more readily available data.

Research on macroeconomics has argued that national accounts "impute" value added in the FIRE sector to make it equal to incomes (wages and profits) (Foley, 2011). In terms of the sector's share of total value added correlated to its share of total employment, finance exhibits a negative (and statistically significant) correlation, while real estate has no significant correlation (Assa, 2016). Financial service revenues represent an opportunity cost, since the money paid for them could have been spent on productive activities elsewhere. The observed negative correlation between the shares of financial services in output and employment has prompted researchers to argue that the FIRE sector is extractive rather than productive (or value reducing rather than value adding) as far as the economy is concerned (Assa 2016, 2017).

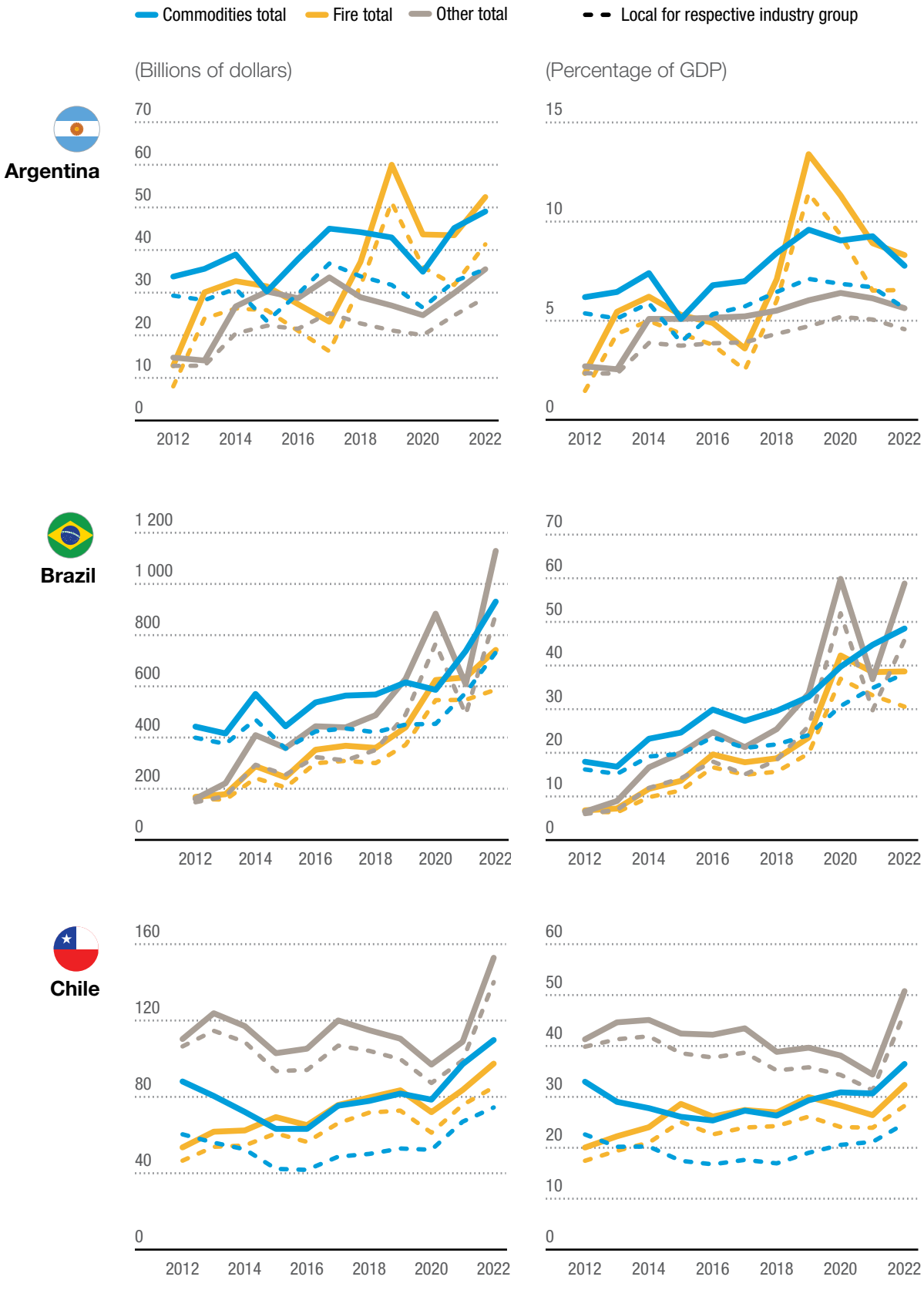
Finance studies have taken the issue further and suggested that, in heavily financialized economies such as the United Kingdom (where the FIRE sector is more than 30 per cent of GDP) and the United States, the reliance on finance for economic growth becomes a drag on the economy, leading to a "finance curse". Analogous to a resource curse, a "finance curse" describes a situation where an outsized financial sector drains resources from other parts of the economy without generating a sufficient share of well-paid jobs and while creating systemic imbalances (Shaxson, 2019; Tax Justice Network, 2020).

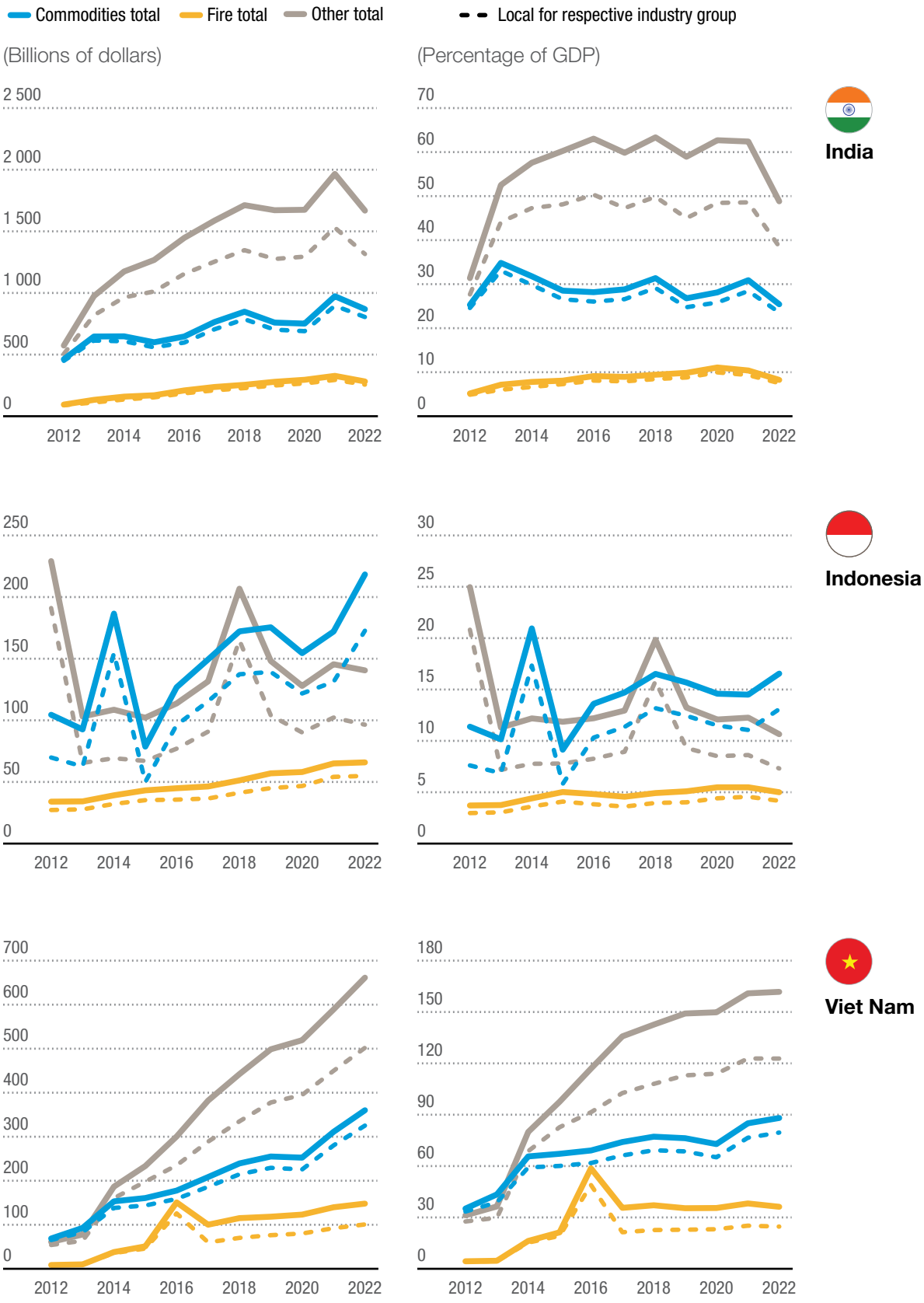
The finance curse has been explored primarily in the context of international financial centres and advanced economies (Baker et al., 2018; Epstein and Montecino, 2016). In the wake of the global financial crisis, Andy Haldane, the then chief economist of the Bank of England, estimated that the costs of "banking pollution" – or the social costs to the public from banking crises – may be close to $100 billion in the United Kingdom (Haldane, 2010). For the economies of the global South, continuing financialization, particularly in the context of the growing role of intangible assets and related financial activities (WIPO, 2024), presents important policy concerns.

To give a glimpse of the issue, figure IV.15 presents the dynamics of sector profits since 2012 for selected developing economies in three key groups of industries: commodities (energy, mining and agriculture), FIRE and the rest of the economy (non-commodities).

Figure IV.15
The extent of economic diversification influences the prominence of the finance, insurance and real estate sector in an economy

Total revenue by industry group, selected countries





Source: UNCTAD based on Orbis database (Moody's).

Notes: An Orbis firm-level classification field delineates commodity, FIRE (finance, insurance and real estate) and "rest of economy" subgroups. Sector groups are aggregated based on financial reports by companies classifying their activities in the relevant sector. The data set includes revenues reported by State-owned enterprises and publicly listed and privately held corporations, including at the subsidiary level.

The figure shows that in countries that have experienced deindustrialization, such as Argentina, Brazil and Chile (Castillo and Neto, 2016), the evolution of revenues in core commodity sectors has become intertwined with the expansion of FIRE sector revenues, particularly during the commodity boom that started in 2020. This has accentuated the risks of instability transmitted through an outsized financial sector, while raising concerns about sector concentration. Figure IV.15 presents a marked contrast with the economies of India, Indonesia and Viet Nam, where economic diversification is more advanced, and the FIRE sector's position and revenue trends appear to be more balanced in the overall structure of the economy.

The finding corresponds with the economic complexity ranking of 133 developing countries published by the Harvard Growth Lab. It calculated the economic complexity of a country based on the diversity of its exports and their ubiquity or the number of countries able to produce them.[35] Overall, the researchers found that the performance of developing countries since 1995 has been mixed (figure IV.16). Some developing countries, particularly in Asia, such as China, India, Indonesia, Malaysia, Singapore, Thailand and Viet Nam, have moved up the ranking very rapidly. But others, particularly economies that have experienced deindustrialization, such as Argentina, Brazil and South Africa, have seen a significant drop in their ranking. This is important in the context of the growing role of service industries and growth, as well as close links and potentially growing interdependencies between financialization and the extractive sectors as described above.

3. Policy focus

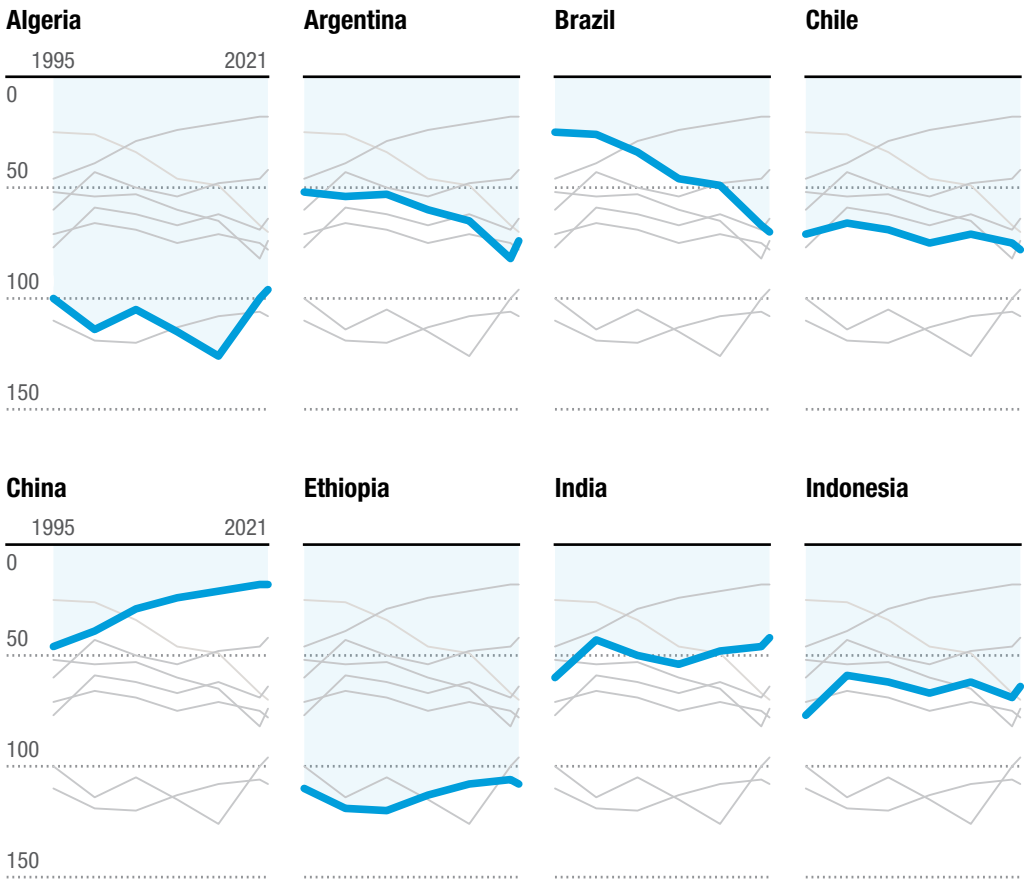
There is limited research on developing countries and the relationship between extractive sectors and financialization, including trade and global value chains (e.g. Cibils and Alami, 2013). Yet with the ongoing consolidation of corporate power over core markets, led by the financial and legal mechanisms of global value chains, this issue needs to come into sharper focus among policymakers across the global South (Lianos et al., 2022; BRICS Competition Law and Policy Centre, 2021).

Left unaddressed by policy, an outsized financial sector (Muda et al., 2020) can add to the problem of commodity dependence in two major ways. First, the unregulated or unbalanced expansion of the finance and finance-centred sectors in commodity-exporting countries can affect sectoral composition within the economy. This can limit economic diversification, undermining resilience and accentuating income inequalities (UNCTAD, 2024c).

Second, in periods of overlapping crises, when turbulence in energy, commodities and financial markets can combine and create multiple points of stress, the effects of the global commodity cycle can be reinforced through a financial sector intertwined with the growth of commodities revenues. In commodity-exporting economies, the expansion of the FIRE sector therefore needs to be considered when devising national industrial and financial regulations and policies (Cibils and Allami, 2013). Closer regulatory attention requires more granular research and understanding of accounting and financial data at all levels of corporate business activities, yet access

[35] "Economic complexity" is a measure of the knowledge in a society as expressed by the products it makes. It is calculated based on the diversity of exports a country produces and their ubiquity or the number of countries able to produce them (and the complexity of those countries). Countries that are able to sustain a diverse range of productive knowledge, including sophisticated, unique know-how, are able to produce a wide diversity of goods, including complex products that few other countries can make (see the Growth Lab definition at https://atlas.cid.harvard.edu/glossary). At the same time, economic complexity cannot be seen as a surrogate for the concept of development, which is a multidimensional process. For example, the economic complexity index ranks of Australia and Norway are quite low due to their trade structure but they are among the most developed economies. For several countries from the global South, such as China, India, Thailand and Viet Nam, although they have rapidly become the main exporters of many sophisticated manufacturing products, various development indicators remain a challenge.

Figure IV.16
Countries that have improved on an index of economic complexity tend to have more diversified economies
Ranking on the economic complexity index, selected countries



Source: UNCTAD based on the Atlas of Economic Complexity. Havard Growth Lab.

to such data remains scarce in many developing economies, especially in Africa.

Safeguarding economic resilience and equity, in turn, calls for coordination of the policies of redistribution, diversification and financial regulation. Crucially, for raising development finance, these measures need to enhance domestic revenue mobilization, including through greater efforts to curb corporate arbitrage, trace and monitor the economic footprint of multinational enterprises, and share relevant data at the multilateral level to enhance policy coordination.

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Chapter V

The global South and new international tax architecture: The quest for development finance

The ongoing initiative to establish the United Nations framework convention on international tax cooperation offers an important opportunity for developing countries to close current gaps in the international financial architecture and embed sources of domestic revenue in their economies.

In contrast to the existing tax regime, which relies on bilateral and limited multilateral tax agreements, the convention aims to create a global multilateral framework for international tax cooperation.

Unlike many earlier global tax proposals, such as taxation of international currency transactions, the proposed convention would be unique in bringing international taxation under a comprehensive framework. It would thus enable a focus on both the trade and financial dimensions of global business activities.

The goal of the convention is to create a global tax platform that would address base erosion and profit-shifting (BEPS) activities, such as tax avoidance and illicit financial flows, and enhance international financial integrity and governance, all of which are key to effective financing for development and the Sustainable Development Goals.

The success and efficacy of the proposed tax architecture for development will depend on policy cooperation among developing countries and global North–South dialogue.

United Nations

Policy takeaways

- While both the United Nations and OECD seek to improve international tax cooperation, the former takes **a more inclusive and transparent approach focused on and representative of the global South**.
- Ongoing negotiations and the potential eventual adoption of the United Nations framework convention on international tax cooperation could play central roles in shaping the future of tax cooperation and reforming the international financial architecture. **Commitment from Member States, careful diplomacy and technical expertise will be key to success**.
- **Risks of the emergence of a differential tax regime globally cannot be ignored.** Double taxation and arbitrage niches can harm global trade and investment flows, endangering domestic revenue mobilization. This is particularly true for consumer-facing and digital economy businesses, given that the bulk of consumers are in developing countries.
- **In the wider quest for sources of long-term development finance, policy efforts in the global South need to focus on the root causes of inadequate public resources for sustainable development**, which include corporate arbitrage, financialization and the concentration of corporate power.

A. Introduction

The current inflection point in globalization accentuates the structural barriers that developing economies face on the path to more inclusive economic integration and sustainable growth. As the fiscal and trade policies of advanced countries shift to support long-term reindustrialization and climate transition at home, global financial markets are focused on maximizing private sector profit (Foroohar, 2024).

In 2023–2024, an important development in global economic governance took root. Following a series of initiatives led by Nigeria and the Group of African States, the United Nations General Assembly in December 2023 approved the creation of an Ad Hoc Committee to Draft Terms of Reference for a United Nations Framework Convention on International Tax Cooperation (Ad Hoc Committee). The committee started its work in 2024.

The proposed framework convention focuses on both the trade and financial dimensions of global business activities.

The proposed convention would establish a new international tax architecture, one providing countries of the global South with greater revenues and stemming what they view as aggressive profit shifting out of their countries. The convention could take a significant step towards closing some current gaps in the international financial architecture by focusing on both the trade and financial dimensions of global business activities. The goal is to create a global tax platform to address BEPS activities, such as tax avoidance and illicit financial flows, and enhance international financial integrity and governance, all of which are key to effective financing for development and the Sustainable Development Goals.

This chapter examines the potential role of the tax convention in a sustainable finance agenda. Section B lays out key markers in the quest for long-term development finance. It focuses on the UNCTAD agenda for a development-conscious international financial architecture and discusses the challenges of domestic revenue mobilization. Section C explores the role of the tax convention in securing long-term finance for development. Section D analyses the potential benefits and challenges for the global South of current proposals at the United Nations and under the OECD inclusive framework process. Section E concludes the chapter.

B. The quest for long-term sources of development finance

As one economist put it, a key reason for the success of the Bretton Woods institutions in the early post-war period was "amazing institutional engineering" (Rodrik, 2011). Today, amid fundamental changes in production, trade, finance, technology and climate, a repositioning of the interests and voices of the global South in global economic governance requires a re-engineering of several dimensions of the global economy. Such a reform should be guided by the core principles of inclusiveness, North–South dialogue and consultation, and safeguards for the policy space of developing countries. Across these three concerns, a core priority is to address deficits in representation in institutions of global economic governance.

The pandemic and cascading crises have hindered progress on the Sustainable Development Goals in the global South. For the first goal, to end poverty, the number of people living in extreme poverty rose to 724 million in 2020, surpassing the pre-pandemic projection by 90 million and reversing approximately three years of progress on poverty reduction. Under current trends, 575 million people will still be living in extreme poverty in 2030, and only about one third of countries will meet the target to halve national poverty levels. In such a context, the countries of the global South need external support, including through multilateral actions to shape a global financial architecture that enables sustained economic growth and achievement of the Sustainable Development Goals.

Developing countries face hard policy trade-offs due to complex and overlapping crises linked to high energy prices, increased demands for health and social services, and constraints on international trade due to rising protectionism and the geoeconomic changes discussed in chapter III. While 54 developing countries still do not have credit ratings and are denied access to financial markets, only a handful of those that do have ratings have reached investment grade. Among countries in Africa and Latin America, 58 have ratings. In 2019, 11 had investment grade ratings, a number that fell to 8 in 2023. Among all developing countries, only 22 had investment grade ratings. High costs, volatile external private financing and limited access to affordable public financing exacerbate already lagging development finance (see chapter II).

International financial reform is becoming more urgent as the debt crisis risks morphing into a development crisis.

The urgency of the reform of the international debt architecture is escalating as debt stresses risk morphing into a development crisis in the global South. The need for a global financial safety net is increasingly acute, as current mechanisms are inadequate in the face of the mounting financial needs of many developing countries (figure V.1). There are also issues of representation and lending capacity within the global financial safety net that policymakers in the global South need to consider (box V.1).

Box V.1
Regional and bilateral measures in times of crises

The global financial safety net plays a key role in supporting countries during major shocks and crises. It offered unprecedented capacity for crisis prevention when the COVID-19 shock occurred in 2020, having expanded tenfold in size over the decade since the global financial crisis.

An evolving element of the global financial safety net entails regional financing arrangements that provide urgent short-term liquidity and foreign exchange coverage on preferential terms, without the austerity and unpopular procyclical conditionalities typically imposed by the IMF. Some of these arrangements also offered parity in governance and equitable voting rights in ways that do not yet exist in the Bretton Woods institutions.

In 2019–2020, regional financing arrangements lent more than $5 billion to their members, a significant sum. In many cases, these arrangements were seen as a "first resort" and complement to the "last resort" of global institutions (Barrowclough et al., 2022; UNCTAD, 2022). Even so, and despite the expanded capacity of regional arrangements, they remained largely untapped during the COVID-19 period. They also provided relatively uneven support (UNCTAD, 2022) to both lower- and higher-income countries (Hawkins and Prates, 2021; Mühlich and Fritz, 2021; Mühlich et al., 2020, 2022).

Bilateral swap arrangements have become a new and rapidly dominating form of finance that was used extensively during the COVID-19 crisis, reaching a total of $1.5 trillion. A wide range of central banks offer swaps, including banks in developing countries such as Bhutan, India, Indonesia, Maldives, Qatar and Sri Lanka, to name a few. Swaps arranged by developing country banks are much smaller than those orchestrated by the United States Federal Reserve and the People's Bank of China, and to a lesser degree by central banks in other advanced economies, such as Australia, Japan, Sweden, Switzerland and the United Kingdom.

Heavy reliance on bilateral swaps was already emerging in the year before the COVID-19 crisis, causing concern (Mühlich et al., 2022; UNCTAD, 2022; Barrowclough et al., 2022) as the effect on the global financial safety net is ambiguous. While such swaps seem to be a voluminous source of finance, in practice, they lack many of the advantages of multilateral global or regional lending – including predictability and transparency. Swaps represent an extreme form of factionalism between two countries rather than the "club" type arrangements by multiple countries that lie at the heart of regional or international financing arrangements. Bilateral schemes are discretionary by definition and design, lack standard practices or protocols, and are neither transparent nor equitably distributed among developing countries.

The IMF remains the global lender of last resort. During the pandemic shock, it provided over $119 billion (Mühlich et al., 2024). Yet despite regular calls for a fundamental reform of the IMF quota system, there was no net increase in lending capacity in the recent sixteenth General Review of Quotas nor a realignment of the system to reflect the needs and economic or demographic weight of developing countries. While quotas increased by 50 per cent, there was a proportional reduction in other sources of IMF finance, including the New Arrangement to Borrow, meaning that IMF lending firepower has effectively remained constant.

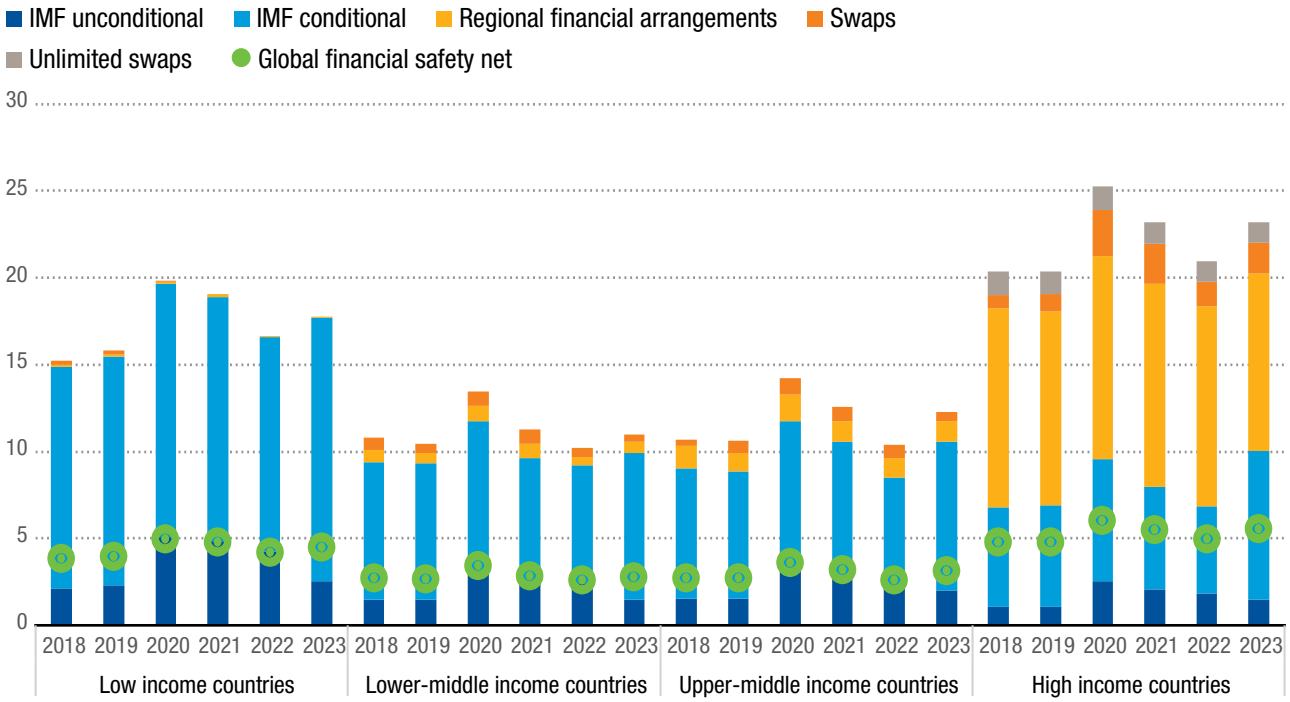
Sources: Barrowclough et al. (2022); UNCTAD (2022); Hawkins and Prates (2021); Mühlich et al. (2020, 2022, 2024); Mühlich and Fritz (2021).

Timely and flexible liquidity, debt relief, sovereign debt restructuring, an expanded global financial safety net and a wider scope for multilateral development bank lending remain top priorities in the multilateral agenda on financing for development. They lie at the heart of reform proposals by UNCTAD to establish a development-conscious international financial architecture (table V.1).

Crucially, these efforts need to take place in parallel with the democratization of the governance structures of the international financial institutions, where developing countries remain underrepresented despite some improvements over the past two decades (figure V.2).[36] Beyond these urgent tasks, long-term development financing requires a foundation of effective and coordinated mechanisms for revenue mobilization.

Long-term development financing requires a foundation of effective mechanisms for revenue mobilization.

Figure V.1
Inequities in access to crisis finance in the global financial safety net
Access to lending facilities by country income group
(Percentage of GDP)



Source: Derived from data from Global Financial Safety Net Tracker available at https://www.bu.edu/gdp/global-financial-safety-net-tracker/. The Boston University Global Development Policy Center, Freie Universitat Berlin and UNCTAD created the tracker as the first global interactive database measuring the annual lending capacity of the IMF, central banks and regional financing agreements, and the total amount of financing to combat the COVID-19 crisis via loans from the IMF, regional financing agreements and currency swaps.

Note: Green dots indicate the averages of all individual components.

[36] At the International Bank for Reconstruction and Development, part of the World Bank Group, for example, developing countries have 43 per cent of the overall vote compared to 38 per cent in 2000. This represents an increase of some 15 percentage points over 24 years. While the level is marginally below the level of the developing country share of global GDP, which is around 40 per cent, it is only half their share in terms of population. In organizations where voting is arranged on a one country, one vote basis, such as the WTO and United Nations, the developing country share is between 60 and 75 per cent of the total vote. This does not mean that decisions are made to their advantage, nor can it be argued that developing countries always vote in the same direction. Individual country interests can vary significantly, just as with advanced countries.

Table V.1
Proposals to reform the international financial architecture

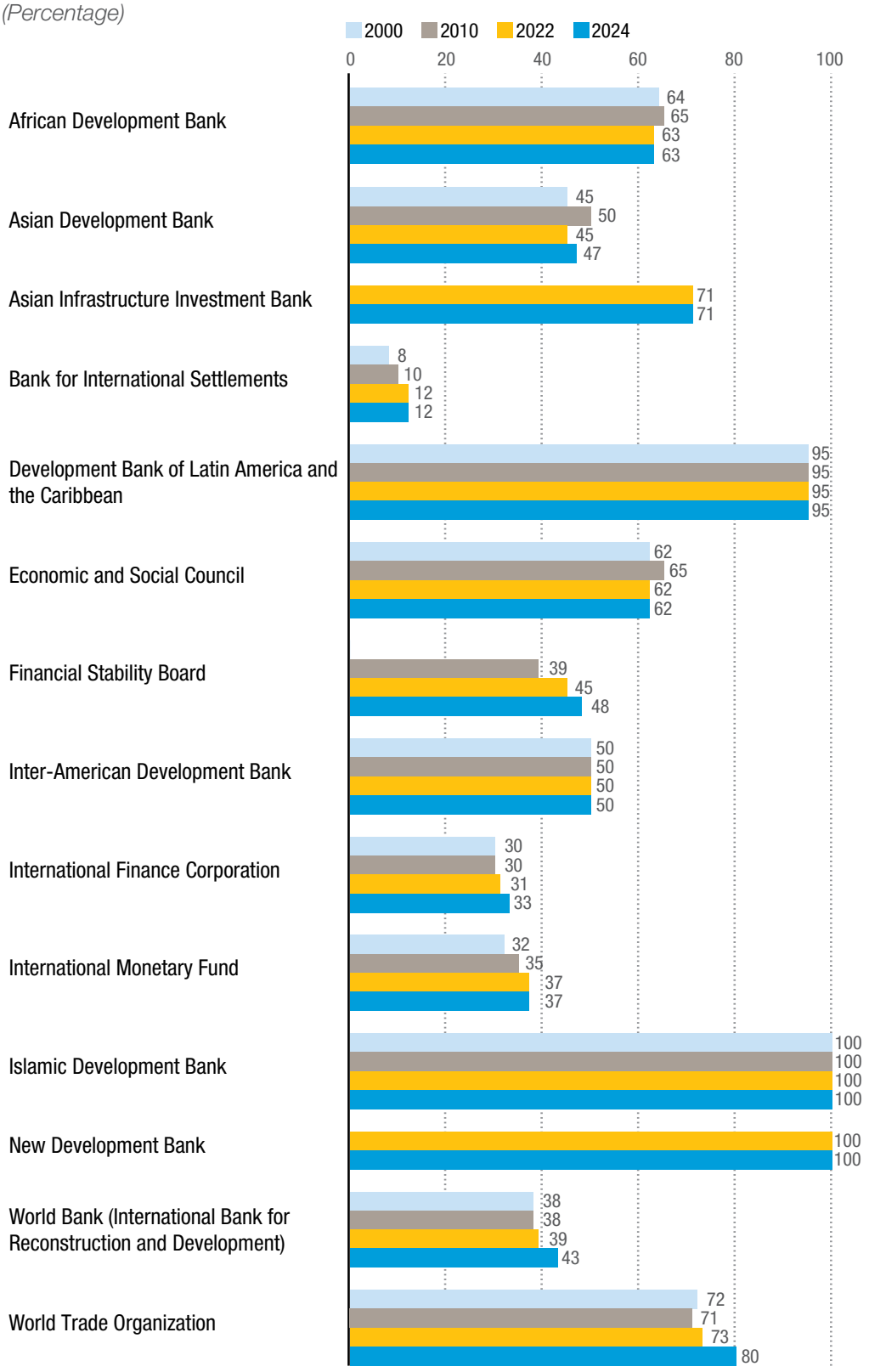
UNCTAD proposals	Related actions recommended by the United Nations in Our Common Agenda Policy Brief 6
Institutional reform	Action 1. Transform the governance of international financial institutions
	Action 2. Create a representative apex body to systematically enhance coherence of the international system
Liquidity **1965**: Universal special drawing rights allocations with aid link **1971**: Creation of the Group of 24	Action 10. Strengthen liquidity provision and widen the financial safety net
	Action 11. Address capital market volatility
Investment **1964**: Multilateral interest equalization fund (Horowitz proposal) **1965**: Universal special drawing rights allocation with aid link **1970**: Official development assistance target of 0.7 per cent of GDP **1971**: Definition of least developed countries **2014**: Support for Southern-led multilateral development banks	Action 5. Massively increase development lending and improve terms of lending
	Action 6. Change the business models of multilateral development banks and other public development banks to focus on sustainable development goal impact; and more effectively leverage private finance for sustainable development goal impact
	Action 7. Massively increase climate finance, while ensuring additionality
	Action 8. More effectively use the system of development banks to increase lending and sustainable development goal impact
	Action 9. Ensure that the poorest can continue to benefit from the multilateral development bank system
Debt **1980**: Trade and Development Board agrees on the need for a Mechanism for Fair Sovereign Debt Workouts **1983**: Creation of the Debt Management and Financial Analysis System **2012**: Principles for Responsible Sovereign Lending and Borrowing **2014–2015**: United Nations General Assembly resolution creating the Ad Hoc Committee on Sovereign Debt Restructuring, definition of basic principles.	Action 3. Reduce debt risks and enhance sovereign debt markets to support sustainable development goals
	Action 4: Enhance debt crisis resolution through a two-step process: a debt workout mechanism to support the common framework and, in the medium term, a sovereign debt authority
Finance–corporate nexus **1967**: United Nations General Assembly resolution creating the Ad Hoc Group of Experts on International Cooperation in Tax Matters. **1975–1993**: Creation of the Centre for Transnational Corporations	Action 12. Strengthen regulation and supervision of bank and non-bank financial institutions to better manage risks and rein in excessive leverage
	Action 13. Make businesses more sustainable and reduce greenwashing
	Action 14. Strengthen global financial integrity standards
	Action 15. Strengthen global tax norms to address digitalization and globalization through an inclusive process, in ways that meet the needs and capacities of developing countries and other stakeholders
	Action 16. Improve pillar two of the proposal by the OECD/Group of 20 inclusive framework on [BEPS] to reduce wasteful tax incentives, while better incentivizing taxation in source countries
	Action 17. Create global tax transparency and information-sharing frameworks that benefit all countries

Source: UNCTAD based on United Nations (2023a), which contains more detailed lists of subactions.

Note: Yellow indicates actions and/or subactions to address the transversal challenges of climate and environmental sustainability.

Figure V.2
Developing country voting rights have shifted only incrementally in major economic governance institutions

Developing country share of voting rights by year and institution
(Percentage)



Source: UNCTAD based on the websites of respective organizations.

Given the constraints and costs of external funding, domestic revenue mobilization through taxes and other means remains the most sustainable source of financing for developing countries.[37] It is a central lever for developing State capacity and maintaining macroeconomic stability, enabling governments to make required investments independent of external sources. The 2030 Agenda aims to "strengthen domestic resource mobilization, including through international support to lower-income countries, to improve domestic capacity for tax and other revenue collection" (Garcia-Bernardo and Janský, 2024).

The international tax system allows significant corporate arbitrage opportunities, enabling tax evasion and avoidance.

Inadequate domestic financing in developing countries holds back progress, including on the Sustainable Development Goals. Many developing countries fall below the 15 per cent tax-to-GDP ratio that most experts agree is the minimum needed to reach the Goals. Especially in low-income developing economies, a narrower tax base, capacity limitations, the preponderance of shadow and informal economies, and governance challenges all play parts in weak domestic resource mobilization.

Asymmetries in negotiating positions over double taxation agreements have left many developing countries vulnerable to base erosion and profit-shifting activities.

While developing countries may not derive substantial revenue from cross-border income flows due to problems in mobilizing resources domestically, there are also concerns that current international tax rules are inadequate for their needs and constrain their ability to expand revenue sources in a globalized and digital economy. Tax authorities often lack tools and technical capacity (e.g. data, personnel and other resources) to adequately tackle BEPS challenges.

In addition, developing countries have fewer double tax agreements. Where such agreements exist and involve advanced countries, a common concern is that treaty negotiators have capacity constraints and asymmetries in negotiating positions that leave developing countries vulnerable to BEPS activities by multinational enterprises.

The current international tax system has provided multinational enterprises with significant cross-border arbitrage opportunities. Such practices, although typically viewed by enterprises and their international tax advisers as ethical and legal tax planning, are regarded by developing countries and non-governmental organizations as unethical and illegal. Tax administrations in developing countries are particularly concerned where multinational enterprises move "over the line" from legal regulatory arbitrage into abusive tax practices (Eden and Smith, 2022). Meanwhile, global profit shifting by multinational enterprises has been encouraged by the rapid growth in the number and sophistication of tax havens and financial hub structures (UNCTAD, 2022).

Estimates of losses due to tax avoidance in developing countries are varied and incomplete. While a United Nations Office on Drugs and Crime and UNCTAD (2020) conceptual framework helps to resolve definitional issues around crime-related illicit financial flows versus mispricing, measurement challenges related to primary data availability remain. Some methodologies are still being tested and refined.

Overall, recent estimates suggest that global profit shifting has severely hampered domestic resource mobilization, particularly in low-income developing countries. Wier and Zucman (2022), for example, estimate that over 2015–2019, nearly 40 per cent of the profits of multinational enterprises were booked in tax havens. Further, profit shifting reduced global corporate income tax revenues by 10 per cent, and the effective global corporate income tax rate fell by one third (Wier and Zucman, 2022). Chiari (2024) estimates that global tax revenue losses in 2019 were $480 billion

[37] On building tax capacity for development, some have argued that broadening the tax base and improving institutions in addition to international cooperation on taxing the profits of multinational enterprises would significantly improve domestic resource mobilization in low-income developing countries (see Benitez et al., 2023).

using statutory corporate income tax rates and $600 billion using effective rates.

A recent review of available case studies suggests that multinational enterprises shift up to 40 per cent ($600 billion to $1.1 trillion) of foreign profits to conduit countries such as Bermuda, the Kingdom of the Netherlands or Switzerland. While in absolute terms the United States suffers most from profit shifting, other advanced economies, such as France and Germany, lose up to half their profit base in this manner (Clausing, 2016; Torslov et al., 2023.

In relative terms, countries with lower incomes lose a larger share of total tax revenue due to profit shifting, even when their revenue losses in absolute terms are smaller. In particular, lower-income countries in Africa and Latin America tend to see more tax revenue disappear relative to total tax revenue. African economies lose a higher share than average. Overall, only a small number of countries gains any tax revenue (Garcia-Bernardo and Janský, 2024).

Corporate arbitrage, or strategic manoeuvring by corporations among different jurisdictional niches, compounds the challenge of revenue mobilization, as well as corporate accountability and transparency. Modern corporate arbitrage practices are widespread and wide ranging. They include regulatory, reporting, tax and accounting arbitrage. Liability avoidance techniques enable multinational enterprises to circumvent social and environmental responsibilities, often imposing the costs of external shocks and crises on the most vulnerable countries (Baines and Hager, 2021; Palan et al., 2023; UNCTAD, 2024). Moreover, corporate arbitrage enables enterprises to minimize their economic footprint in many developing economies. A recent study found that one quarter of the subsidiaries of the top 100 non-financial multinational enterprises in the global South engaged in no apparent associated economic activity (UNCTAD, 2022).

The phenomenon of illicit financial flows further compounds the challenges of revenue mobilization in the global South. Ongoing pilot studies of selected developing countries by UNCTAD find that extractive industries tend to be particularly prone to such flows through trade misinvoicing and profit shifting (table V.2). Examples include beverages, petroleum and ore in Burkina Faso, and precious metals and stones and electrical machinery in South Africa. Burkina Faso has found illicit financial flows in the gold sector with transactions involving Switzerland and Uganda. Nigeria examined profit shifting in the petroleum sector, revealing flows to tax havens. Early estimates suggest that illicit flows may total up to half of officially recorded trade.

Extractive industries are particularly prone to illicit financial flows through trade misinvoicing and profit shifting.

Lower-income countries lose a larger share of total tax revenue due to profit shifting.

Given these challenges, developing countries have long sought a United Nations-centred approach to international tax cooperation, one where they have equal standing. International tax cooperation at the United Nations is perceived as a key component for improving domestic resource mobilization, especially in low-income developing countries. The proposed United Nations framework convention on international tax cooperation is thus seen by many developing countries as part of rebalancing the international financial system so that it operates on a fairer basis.

The proposed convention is the first attempt to create a global multilateral framework for international tax cooperation. The current tax architecture relies on bilateral and limited multilateral agreements. While a range of global proposals for tax arrangements has been put forward, such as taxation of international currency transactions, the proposed tax convention is unique because it would bring international taxation under a comprehensive framework.

Table V.2
Early estimates suggest illicit financial flows may comprise up to 50 per cent of official trade in some economies

Unofficial preliminary estimated tax and commercial illicit financial flows (inward and outward), selected African countries

Country	Year(s) covered	Period length (Number of years)	Estimation method(s)	Tax and commercial illicit financial flows as shares of official trade (Percentage, annual average)
Ghana	2000–2012	13	PCM+ and PFM+	5.1
Burkina Faso	2011–2020	10	PCM+	10.5
Zambia	2012–2020	9	PCM	30.2
South Africa	2017	1	PCM+	32.7
Gabon	2010–2021	12	PCM+ and PFM+	50.5
Namibia	2018–2020	3	PFM+	57.1

Source: UNCTAD based on United Nations Economic Commission for Africa (2023).

Notes: This figure shows early unofficial estimates resulting from 2021–2022 country pilots using different methods to measure tax and commercial illicit financial flows from trade misinvoicing. Early estimates will likely be refined and extended by national authorities in the future. The methods used for estimations are the partner country method plus (PCM+) and the price filter method plus (PFM+). See the UNCTAD SDG Pulse for more information on efforts to track illicit financial flows, available at https://sdgpulse.unctad.org/illicit-financial-flows/.

C. The global South and the call for an international tax architecture

For more than 60 years, the OECD, led by the global North, has set the rules by which States tax multinational enterprises. Under these rules, profits have been allocated among countries through hundreds of bilateral tax treaties, usually called double taxation agreements. These agreements allocate taxing rights based on complex residence- and source-based principles, and price intercorporate transactions according to the arm's length principle.[38] The use of double taxation agreement networks to manage international tax relations came out of the work of the League of Nations in the 1920s (League of Nations, 2023).

Developing countries emerging from colonial rule in the 1960s and 1970s strongly expressed their need for a new and more equitable international economic order. In particular, UNCTAD and the Group of 77 and China were central forums for discussions of this issue. In the late 1960s, the Ad Hoc Group of Experts on Tax Treaties between Developed and Developing Countries was formed as part of the same debate.[39]

There have been many criticisms of double tax agreements, especially by developing countries. First, they are viewed as primarily preventing double taxation, where profits are taxed by both residence and source countries, with less attention paid to preventing double non-taxation, where enterprises use tax evasion and aggressive tax avoidance techniques to avoid paying taxes in either residence or source countries.

Second, double tax agreements are viewed by many as favouring capital-exporting (residence) countries at the expense of capital-importing (source) countries.[40] Third, the complexity of these agreements has created many tax loopholes that have fostered BEPS activities. In general, while the broad principle of preventing double taxation is valid, advanced economies have been the main beneficiaries of double tax agreements. Such agreements have not been a major driver of foreign direct investment in developing countries.

Over the last quarter century, developing countries have intensified their focus on international tax cooperation. As capital-exporting countries shifted from worldwide to territorial taxation, significant differences in tax rates and bases across countries provided many opportunities for sophisticated tax planning. With the

Double taxation agreements do not prevent double non-taxation and favour capital-exporting countries.

[38] Historically, source and residence principles have determined which country (home or host) has the primary right to tax different multinational enterprise revenue streams (e.g. royalties and service fees). Where both countries have taxing rights (e.g. over foreign affiliate profits), the "first crack" principle gives the first taxing rights to the host country, with the home country (if it chooses to tax foreign source income) having to provide tax room through a foreign tax credit or deduction. The arm's length principle ensures that related party transactions and activities are priced based on what independent enterprises would have done under the same or similar facts and circumstances. See chapter 2 in Eden (1998).

[39] Economic and Social Council resolution 1273 (XLIII) of 4 August 1967. As illustrated by the group's title, the focus was still on an international tax system managed through double tax agreements. Since 11 November 2004, the group has been known as the Committee of Experts on International Cooperation in Tax Matters (the United Nations Tax Committee).

[40] Net capital exporters are usually assumed to be developed countries and net capital importers to be developing countries. In the twenty-first century, however, most developed countries have two-way foreign direct investment flows; many are net capital importers, in both stock and flow terms. Still, when considering flows and stocks between pairs of countries, with certain exceptions (e.g. investment hubs or tax havens), the net capital exporter is typically the more developed economy. Eyitayo-Oyesode (2020) argues that several articles in the OECD Model Tax Convention favour residence-based taxing rights and are therefore biased against developing countries.

international tax architecture riddled with loopholes, multinational enterprises used aggressive profit-shifting strategies to move profits into tax havens and investment hubs. The rising number of tax havens and offshore financial centres encouraged both legal and illicit capital flows, as documented by UNCTAD (2015).

In addition, the growing number of digital multinational enterprises and "industry 4.0" created a world of "scale without mass" built on automated digital services and transactions and hypermobile capital flows. These opened new paths to take advantage of BEPS opportunities (box V.2).

Box V.2
The OECD and the two-pillar process

The global financial crisis of 2008–2009 was probably the final tipping point in Governments realizing that multilateral, not bilateral, efforts were needed to counteract BEPS activities (Mason, 2020).

The OECD 2012–2015 BEPS project subsequently resulted in 15 action items to fill loopholes seen as primary BEPS factors. These items were designed, in part, to shift double taxation agreements from mainly preventing double taxation to also eliminating double non-taxation. The changes included country-by-country reporting and a new multilateral tax instrument, the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting. The latter was designed to apply alongside a country's existing double taxation agreements and to modify them by allowing signatories to adopt the action items without having to renegotiate agreements. Many Governments, including the United States, have not signed the multilateral tax instrument, however, and many signatories have opted out of key provisions.[a]

The OECD had left the first action item, on taxing the digital economy, for later work, but progress was slowed by the COVID-19 pandemic. Through its inclusive framework process[b] in the second BEPS round, the OECD and members of the Inclusive Framework have proposed to replace or overlay some current international tax rules with fundamentally different ones. A "two-pillar process" includes a new tax on the profits of the world's 100 largest multinational enterprises (Pillar One Amount A) and a new global minimum profit tax of 15 per cent on almost all multinational enterprises (Pillar Two Global Anti-Base Erosion Model Rules).[c]

The proposed new policies are significantly more complex and mostly untested. While some Governments have begun implementing the global minimum tax rules, there is no current agreement on pillar one, with criticisms centring on its complexity, non-compliance with existing international tax principles (e.g. the arm's length principle),

[a] Current information on signatories is in the OECD database on the multilateral tax instrument, available at https://www.oecd.org/tax/treaties/mli-matching-database.htm.

[b] The inclusive framework is an attempt by the OECD to overcome its "democratic deficit" by bringing in non-member countries to achieve consensus on these rules. Critics say the framework is flawed since it essentially works with a menu set by the OECD. Many developing countries, but not all, are framework members. See https://www.oecd.org/en/topics/policy-issues/base-erosion-and-profit-shifting-beps.html.

[c] For example, pillar one replaces the arm's length principle with a global formulary apportionment; see Eden (2022). A second example is the income inclusion rule in pillar two, whereby the right to levy a top-up tax on undertaxed profits was given first to the residence country under the income inclusion rule, rather than following the "first crack" principle. While a domestic top-up tax was later added, which could be credited against the income inclusion rule, restrictions on the domestic top-up tax still tilt the balance in favour of residence countries.

Box V.2 The OECD and the two-pillar process

alack of clear benefits for developing countries and failure to adequately address the problems of taxing the digital economy. Moreover, the proposed OECD multilateral convention to implement pillar one is unlikely to be adopted, given its ratification requirements.[d] As a result, developing countries have viewed the second BEPS round with suspicion. Most are not OECD members and see themselves primarily as bystanders in the process.[e]

Source: Mason (2020).

[d] At least 30 countries representing around 60 per cent of ultimate parent entities of in-scope multinational enterprises under pillar one must ratify the convention. See https://www.oecd.org/en/topics/sub-issues/reallocation-of-taxing-rights-to-market-jurisdictions/multilateral-convention-to-implement-amount-a-of-pillar-one.html.

[e] See also the comments on problems with the effectiveness and inclusiveness of the OECD BEPS process in the report of the United Nations Secretary-General on the promotion of inclusive and effective international tax cooperation at the United Nations (A/78/235).

D. Developing countries push for a United Nations-led convention

Dissatisfaction has continued to grow with the current international tax system as developing countries have sought to establish a process that would allow all countries to participate on an equal footing in decision-making related to tax. As far back as 2012, the Group of 77 and China, with the support of advocacy groups, have attempted, with limited success, to jumpstart an intergovernmental tax negotiation process at the United Nations.[41] For many years, the Group of African States advocated a United Nations-centred international tax convention. The United Nations Tax Committee has held regular special sessions at the Economic and Social Council on international tax cooperation.[42]

A key event was a 2015 proposal by developing countries for a United Nations body to address international tax cooperation as part of the Addis Ababa Action Agenda.[43] The proposal was not accepted but the United Nations agreed to further its efforts in international tax cooperation. In October 2022, the Group of African States proposed a United Nations General Assembly resolution on illicit financial flows that included creating a United Nations intergovernmental tax body. Some non-governmental organizations prepared early proposals for a framework convention.[44]

A breakthrough came when the Group of African States tabled a revised proposal

[41] See the list of statements by developing countries calling for a United Nations-led process on international tax cooperation, complied by the Civil Society Financing for Development Mechanism in a database available at https://csoforffd.org/post/database-governments-supporting-an-intergovernmental-un-tax-body-and-or-un-tax-convention/. The 2012 statement by the Group 77 and China is available at http://www.g77.org/statement/getstatement.php?id=120727.

[42] Special sessions go back at least to 2019; see https://financing.desa.un.org/ecosoc-special-meeting-international-cooperation-tax-matters.

[43] The Addis Ababa Action Agenda of the Third International Conference on Financing for Development is available at https://sdgs.un.org/documents/ares69313-addis-ababa-action-agenda-thi-21093.

[44] For two early proposals for a framework convention, see Chowdhary and Picciotto (2021); Ryding (2022).

that became resolution 77/244,[45] approved by the General Assembly without a vote on 23 November 2022. The resolution asked the United Nations Secretary-General to outline possible steps to strengthen the inclusiveness and effectiveness of international tax cooperation and invite interested parties to provide inputs. Multiple submissions were made by Member States, non-governmental organizations, academics, think tanks and the business community. The International Bureau of Fiscal Documentation (2023) and the International Centre for Tax and Development (Cadzow et al., 2023) prepared reports.[46]

The Secretary-General issued a report that concluded that the OECD inclusive framework two-pillar process did not take the needs of developing countries sufficiently into account, and emphasized the need for inclusiveness, where all countries could participate in agenda-setting, negotiations and decision-making (United Nations, 2023). The report noted that the decision-making process should be transparent and provide sufficient time for consideration of proposals and the preparation of positions. The report outlined and discussed three possible options for the United Nations to move forward on international tax cooperation: a forum for non-binding discussions, a binding legal framework convention and protocols or a comprehensive binding legal agreement. It invited input from outside stakeholders.

At the United Nations General Assembly meeting on 15 November 2023, Nigeria, on behalf of the Group of African States, proposed a draft resolution recommending the second option of a framework convention with protocols, along with the creation of an ad hoc committee to draft terms of reference for the convention.

Resolution 78/230 was adopted on 22 December 2023 with a vote of 111 to 46 with 10 abstentions; almost all developing countries voted "yes" and almost all OECD members opposed the resolution.[47] It established the Ad Hoc Committee to Draft Terms of Reference for a United Nations Framework Convention on International Tax Cooperation. It consists of a chair, 18 vice-chairs and a rapporteur;

[45] See United Nations General Assembly resolution 77/244 on the promotion of inclusive and effective international tax cooperation at the United Nations.

[46] The International Bureau of Fiscal Documentation report suggested adaptation of the BEPS minimum standards, simplification of other BEPS recommendations, improvement of the two-pillar solution and so on, essentially working within the OECD inclusive framework process. The International Centre for Tax and Development report focused on the capacity limitations of participating countries and other organizational issues.

[47] See United Nations General Assembly resolution 78/230 on the promotion of inclusive and effective international tax cooperation at the United Nations.

they together represent four members from each of the five regions in the United Nations system. The resolution requested the committee to consider simultaneously developing early protocols in specific priority areas, including tax-related illicit financial flows and taxation of income from cross-border digital services. The committee was asked to prepare the terms of reference by August 2024 and submit a report with them to the seventy-ninth session of the United Nations General Assembly in October 2024.[48] Diverse public comments were submitted on both resolution 78/230 and the agenda for the committee's first meeting.[49]

1. The United Nations Ad Hoc Committee to Draft Terms of Reference for a United Nations Framework Convention on International Tax Cooperation

Framework conventions offer a useful, incremental approach to international lawmaking whereby Governments set up a general system of international governance on a particular issue and then develop more specific commitments and institutional arrangements through protocols (Bodansky and WHO, 1991). In effect, a framework convention creates an "umbrella" or "framework" that is a legally binding multilateral instrument, consisting of core components (e.g. objectives, principles and governance structure) that guide a variety of protocols with opt-in and opt-out clauses. The proposed framework tax convention is set up along similar lines.

Five priority areas for early protocols were identified in June and July 2024 draft terms of reference for the convention: taxation of the digital and globalized economy, taxation of income derived from cross-border services, tax-related illicit financial flows, prevention and resolution of tax disputes, and taxation of high-net-worth individuals. Four other areas were listed as possible subjects for future protocols: tax measures on environmental and climate challenges, exchanges of information for tax purposes, mutual administrative assistance on tax matters and harmful tax practices.

The August 2024 terms of reference reduced the list of early protocols to two, both from the original list: taxation of income from cross-border services and one other to be determined later; the list of other areas remained unchanged. The deadline for adoption of the convention was extended to 2027, with the Ad Hoc Committee to Draft Terms of Reference for a United Nations Framework Convention on International Tax Cooperation continuing to meet at regular intervals. A vote to adopt the terms of reference passed based on an informal tally of 110 to 8, with 44 abstentions.[50]

2. Potential benefits for developing countries

Many developing countries see the proposed framework tax convention as part of their strategy to overcome the asymmetries of capacity and economic development in negotiating with advanced countries to achieve what they see as their fair share of revenues from international trade and investment flows. The convention, when viewed together with ongoing work

[48] The United Nations Tax Committee functions independently from the Ad Hoc Committee to Draft Terms of Reference for a United Nations Framework Convention on International Tax Cooperation. Members of the former serve on the latter in their personal capacities; however, many are now also representing their governments in the work of the Ad Hoc Committee.

[49] For comments on resolution 78/230, see https://financing.desa.un.org/un-tax-convention/inputs.

[50] See Travers (2024). The formal tally was released on 27 September 2024. The eight negative votes were the "five eyes" (Australia, Canada, New Zealand, United Kingdom and the United States) and Israel, Japan and the Republic of Korea. Most Western European countries switched from no votes in December 2023 on resolution 78/230 to abstentions in August 2024 on the draft terms of reference.

The framework convention can help build a more equitable, inclusive international tax regime.

at the United Nations Tax Committee,[51] could potentially bring together existing international tax relationships and guidance so that the benefits of past work are retained within the new framework. The framework convention and its protocols offer developing countries the opportunity to build a more equitable and inclusive international tax regime, one that can provide support to overcome capacity and governance challenges.

The OECD also offers some assistance on policy matters and works with the United Nations Development Programme to deliver capacity improvements in tax administration. Yet the OECD ignores, in the view of many observers, the development dimensions of tax and is often seen as overly concerned with detailed technical issues.

Developing countries tend to view the OECD inclusive framework process as essentially a forum for developed countries. While there are issues of common concern regarding taxation of the digital economy, perspectives and approaches differ. Developing countries also have different approaches to issues around illicit financial flows, while domestic resource mobilization targets are not a pressing issue in many OECD member States. The existing "competing frameworks", in the view of many developing countries, lack their informed consent and are influenced by the dynamics of bilateral relationships.

When evaluating the effectiveness of the proposed framework convention and, in particular, focusing on the policy space of developing countries envisioned by new norms, the following factors can be considered:

- **Inclusivity and representation.** The United Nations framework convention aims to be more inclusive, giving equal voice to developing and developed countries, whereas the OECD two-pillar process has been criticized for being dominated by OECD member States. Inclusivity is necessary to create a fairer, more democratic and effective global tax system.
- **Decision-making process.** The United Nations framework convention would likely operate on the basis of a majority vote by United Nations Member States, which may make it easier to adopt certain measures. The OECD inclusive framework approach officially seeks consensus decision-making but does move ahead where consensus is challenging (e.g. the proposed framework convention on pillar one).
- **Scope and focus.** The United Nations approach aims to place greater emphasis on issues important to developing countries, such as taxing profits earned on cross-border services and a larger role for source-based taxation; these topics have received little attention in the two-pillar process. Taxing automated digital services profits, for example, was part of the original pillar one proposal, but this was later replaced by a proposal to tax approximately 100 multinational enterprises. The United Nations Tax Committee, on the other hand, proposed adding an article to the United Nations model tax convention to enable source countries to levy a withholding tax on gross profits on digital services.[52]
- **Transparency.** United Nations negotiations are conducted with a higher level of transparency, with proceedings livestreamed and open to observers. OECD inclusive framework negotiations have traditionally been more secretive. Procedures have been established for interested parties (e.g.

[51] The negotiating body for the framework convention will be a subsidiary body of the United Nations General Assembly. While there will be no direct link between it and the United Nations Tax Committee, overlaps are likely, such as in terms of the so-called fast-track instrument as well as comprehensive technical guidance on transfer pricing, carbon taxation, taxation of extractive industries, etc. See the website of the United Nations Tax Committee at https://financing.desa.un.org/what-we-do/ECOSOC/tax-committee/tax-committee-home.

[52] The August 2024 draft terms of reference list taxing digital services as the first protocol to be developed under the proposed framework tax convention.

intergovernmental organizations, civil society, academic institutions, the private sector, etc.) to participate as observers in the Ad Hoc Committee's work on the terms of reference. Observers do not attend OECD inclusive framework meetings but consult separately.

- **Legitimacy and norm-setting.** Proponents assert that the United Nations has unique legitimacy for collective norm-shaping through an intergovernmental process that considers the needs of countries at different development levels. This is seen as superior to technical guidance from institutions such as the IMF or World Bank.
- **Addressing the failures of existing systems.** Advocates point to the failure of current OECD-led efforts to prevent BEPS activities and address the digital economy. They argue that a United Nations framework is needed to tackle these issues in the digital economy and mobilize resources for development more effectively. A United Nations-led approach could also restore original international tax principles such as the "first crack" principle.
- **Linking to broader goals.** Supporters highlight how a United Nations tax convention could link international tax policy directly to other commitments such as the Sustainable Development Goals, human rights and environmental protection.
- **Flexibility and gradual approach.** Proponents stress that the framework convention model allows for a stepwise approach, defining central objectives and mechanisms while allowing the system to develop more comprehensively over time. Multiple protocols under the umbrella of the proposed convention would be developed to handle specific areas, such as illicit financial flows.
- **Potential for progressive alliances.** The United Nations process could provide an opportunity for new alliances to form across traditional divides: for example, by bringing together developing countries and small open OECD member countries that are primarily host countries to inward foreign direct investment. Both share common interests with respect to the primacy of source-based taxes and the need for withholding taxes on capital outflows.
- **Legally binding nature.** The framework convention would be legally binding and could provide a more formal and enforceable structure compared to existing arrangements.
- **Capacity-building and technical assistance.** There are provisions in the terms of reference for the tax convention where it could potentially include mechanisms for enhancing domestic resource mechanism and building tax capacity in developing countries.
- **More attention to national sovereignty concerns.** The convention could provide a two-track mechanism, similar to Part IV of the General Agreement on Tariffs and Trade on special and differential treatment, with reduced commitments for low-income developing countries. In addition, the convention could allow "fast-track" mechanisms comparable to preferential trading arrangements under the General Agreement on Tariffs and Trade, whereby like-minded countries could deepen bilateral or regional tax integration as long as integration mechanisms do not unduly harm other convention signatories.

3. Key challenges in developing a framework tax convention

The United Nations faces multiple challenges in developing a framework tax convention.[53] Some advanced OECD countries, for example, the eight countries that voted against the August 2024 terms of reference, are resisting an ambitious

[53] On some of the challenges, see Choudhury (2024).

framework convention, preferring to maintain the dominant role of the OECD in setting international tax rules. They argue that existing mechanisms are sufficient and fear that a United Nations-led process might shift the balance of power towards developing countries, which could lead to rules that are less favourable to the interests of more developed nations.[54]

Several areas of disagreement between the OECD inclusive framework and the United Nations process can be identified.

- **Scope and focus.** There are differing views on issues the convention should address. OECD countries want to focus on less controversial topics, while countries of the global South are pushing for the inclusion of all relevant issues, even if previously addressed in other forums.
- **Potential duplication.** Critics argue that a United Nations-led process would duplicate existing efforts by the OECD, which has been the primary body for international tax cooperation since the early 1960s. The OECD has developed comprehensive frameworks and guidelines (e.g. the multilateral convention under the original BEPS round) that are already implemented globally. Supporters of the United Nations convention argue that this is the first time a legally binding framework on international tax cooperation is being negotiated in a truly universal and inclusive forum, and that no duplication as such exists. Rather than duplicating existing processes, they contend the United Nations process would leverage existing strengths while addressing gaps and weaknesses in the international tax system.
- **Risk of fragmentation.** Critics warn that if the United Nations addresses issues dealt with by other international organizations, there will be a risk of duplication and parallel frameworks: for example, one led by the OECD and another by the United Nations, which would fragment international tax rules. This would complicate compliance by multinational enterprises and potentially lead to inconsistencies in tax policy. Proponents, on the other hand, argue that the United Nations process would create a more coherent overall system and could incorporate and build on existing efforts in other forums. Moreover, developing countries stress that it is a matter of their national sovereignty in terms of where to apply their resources.
- **Allocation of resources.** Opponents contend that establishing a new framework would require significant resources that could be better utilized elsewhere. They argue that the financial and administrative burden of participating in another multilateral forum could detract from efforts to meet the Sustainable Development Goals and other critical initiatives. On the other hand, the advantage of negotiating at the United Nations is that each country's permanent mission can assist in negotiations.
- **Complexity and inefficiency.** Another criticism is that the United Nations process might add layers of complexity and inefficiency to international tax governance. The consensus-based approach of the OECD, while sometimes slow and often dominated by its largest member countries, is seen as more streamlined compared to the United Nations. Supporters argue, however, that the United Nations process is likely to produce simpler solutions that are easier to administer and geared to less-resourced countries and situations.
- **Expertise concerns.** Critics of the framework convention argue that the OECD has decades of experience in international tax policy, while United Nations expertise is more limited. The established track record of the OECD makes it better suited to handle complex

[54] The switch in voting of most OECD member countries from "no" on resolution 78/230 to "abstain" on the August 2024 terms of reference suggests that some OECD members may see potential benefits from a United Nations-led process. This might be the case, for example, for those that are primarily capital importers.

tax issues. Proponents, however, note that members of the United Nations Tax Committee and its many subcommittees, although they serve in their personal capacities, are primarily drawn from national tax and finance administrations around the world. Thus, the United Nations already has strong capabilities in terms of international tax experts who have worked together, often for years, on complex international tax issues and problems, especially focused on developing countries.

- **Balancing interests.** The United Nations must navigate competing priorities between advanced and developing nations to create an acceptable framework. Achieving consensus on tax matters is inherently difficult due to differing national interests. Some argue that the inclusive approach of the United Nations might make it harder to reach agreements, as it involves a broader range of stakeholders with varying priorities. If the United Nations is able to balance these competing interests and priorities, however, the stability of the international tax architecture should improve, which would benefit both Governments and the private sector. United Nations-based solutions are also likely to be more legitimate and successful over time.

4. In sum, two ways forward

Proponents view the proposed framework convention as a necessary, inclusive and potentially transformative approach to addressing longstanding issues in global tax governance that existing institutions and processes have failed to adequately resolve. While both OECD and the United Nations seek to improve international tax cooperation, the latter has a more inclusive and transparent process that is focused on and representative of the global South.

The traditional divergence between developing and developed countries on setting global tax policy norms continues, albeit now in a formalized setting. Greater inclusiveness may be achieved through intergovernmental discussions under the United Nations umbrella, and the prioritization of topics and agenda-setting will be subject to more voices and debate than is the case in the OECD inclusive framework process. The OECD secretariat's efficiency and speed in churning out documents in the inclusive framework process cannot be matched by developing countries, leaving many Governments with little time or resources to do more than place a "rubber stamp" on their review. Discussions in the United Nations General Assembly and at the Ad Hoc Committee's meetings in 2024 indicate that the United Nations process moves at a slower pace with more time available. Thus, while it may take longer and seem unwieldy, from the perspective of developing countries, there is a greater chance that new norms will be widely accepted.

Although the United Nations process may take longer, it offers a greater chance that new norms will be widely accepted.

The current negotiations suggest strongly differing views among United Nations Member States on several issues. This was, to some extent, predictable, given the long-standing preference by developed nations to use the OECD platform for dialogue on the global tax architecture. Overcoming these challenges will require careful diplomacy, compromise and a commitment from Member States to create a more inclusive system of international tax cooperation. The influence of broader geopolitical considerations, hitherto absent from tax dialogue, cannot be ignored, given current tensions in global trade and finance.

An important factor will be the position of upper-middle-income countries. Some are already major capital exporters, while others are beginning to see resident firms look for investment opportunities abroad. The importance of such alternative sources of capital is likely to increase at the current inflection point in globalization.

As trade and investment flows increase between the BRICS and other middle-income nations, and from such countries

The divergence between developing and developed countries on setting global tax policy norms continues in a formalized setting.

A key factor in United Nations tax negotiations will be the position of upper-middle-income countries.

to the rest of the developing world, a tax framework agreed by countries on both sides of such flows would be more relevant. Among BRICS nations, China, India and South Africa have been strong voices on behalf of the global South in the work at the United Nations. Brazil has contributed significantly to specific areas.

The establishment of a framework tax convention would have major implications for global tax governance, potentially reshaping international tax policies and practices for decades ahead. The ongoing negotiations and the expected eventual adoption of the convention, together with protocols adopted both simultaneously and later on, will play crucial roles in shaping the future of international tax cooperation and reforming the financial architecture.

The risks of double taxation and arbitrage could jeopardize domestic resource mobilization.

There are risks, too. There could be significant challenges if different regimes were to develop, in which tax relationships among the majority of countries are governed by the United Nations convention while OECD countries and some other high-income countries continue to subscribe to the two-pillar solution. The risks of double taxation and opportunities for arbitrage could affect both global trade and investment flows and jeopardize important domestic resource mobilization considerations.

This is particularly true in the case of consumer-facing and digital economy businesses, where the bulk of consumers are in developing countries. For example, the OECD Pillar One Amount A is designed not only to replace digital services taxes but also to punish countries that continue to implement them. The United Nations framework convention, on the other hand, is likely to include source-country taxation of digital services. The likely result of two different regimes for taxing digital services would be double taxation of the profits of multinational enterprises and reduced foreign direct investment.

E. Conclusion

By adopting a development approach to taxation, the proposed framework tax convention has strong potential to overcome current gaps in global trade and financial governance. It opens an important opportunity to reduce disparities in the international financial architecture and to embed mechanisms for domestic revenue mobilization in the economies of developing countries.

The success and efficacy of the proposed tax architecture will depend on policy cooperation among developing countries, their ability to capitalize on available technical expertise and knowledge networks within the United Nations, and constructive global North–South dialogue. Supported by other reforms discussed above, the convention could be a step towards a more development-conscious international financial architecture.

For this initiative to succeed in the quest for sources of long-term development finance, policy efforts in the global South also need to focus on the root causes of the inadequacy of public resources for sustainable development, including corporate arbitrage, financialization and the concentration of corporate power.

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